PRESIDENT'S FISCAL YEAR 1996 BUDGET

HEARINGS

BEFORE THE

COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES

ONE HUNDRED FOURTH CONGRESS

FIRST SESSION

FEBRUARY 7, 8, AND 9, 1995

Serial 104–25

Printed for the use of the Committee on Ways and Means

U.S. GOVERNMENT PRINTING OFFICE

91–827 CC WASHINGTON : 1996

For sale by the U.S. Government Printing Office
Superintendent of Documents, Congressional Sales Office, Washington, DC 20402
ISBN 0-16-052173-4

COMMITTEE ON WAYS AND MEANS

BILL ARCHER, Texas, *Chairman*

PHILIP M. CRANE, Illinois
BILL THOMAS, California
E. CLAY SHAW, JR., Florida
NANCY L. JOHNSON, Connecticut
JIM BUNNING, Kentucky
AMO HOUGHTON, New York
WALLY HERGER, California
JIM McCRERY, Louisiana
MEL HANCOCK, Missouri
DAVE CAMP, Michigan
JIM RAMSTAD, Minnesota
DICK ZIMMER, New Jersey
JIM NUSSLE, Iowa
SAM JOHNSON, Texas
JENNIFER DUNN, Washington
MAC COLLINS, Georgia
ROB PORTMAN, Ohio
PHILIP S. ENGLISH, Pennsylvania
JOHN ENSIGN, Nevada
JON CHRISTENSEN, Nebraska

SAM M. GIBBONS, Florida
CHARLES B. RANGEL, New York
FORTNEY PETE STARK, California
ANDY JACOBS, JR., Indiana
HAROLD E. FORD, Tennessee
ROBERT T. MATSUI, California
BARBARA B. KENNELLY, Connecticut
WILLIAM J. COYNE, Pennsylvania
SANDER M. LEVIN, Michigan
BENJAMIN L. CARDIN, Maryland
JIM McDERMOTT, Washington
GERALD D. KLECZKA, Wisconsin
JOHN LEWIS, Georgia
L.F. PAYNE, Virginia
RICHARD E. NEAL, Massachusetts

PHILLIP D. MOSELEY, *Chief of Staff*
JANICE MAYS, *Minority Chief Counsel*

CONTENTS

PRESIDENT'S FISCAL YEAR 1996 BUDGET

TUESDAY, FEBRUARY 7, 1995

HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
Washington, D.C.

The committee met, pursuant to notice, at 10:55 a.m., in room 1100, Longworth House Office Building, Hon. Bill Archer (chairman of the committee) presiding.

[The advisories announcing the hearings follow:]

ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

FOR IMMEDIATE RELEASE   CONTACT: (202) 225-1721
January 30, 1995
No. FC-5

ARCHER ANNOUNCES HEARINGS ON PRESIDENT'S FISCAL YEAR 1996 BUDGET

Congressman Bill Archer (R-TX), Chairman of the Committee on Ways and Means, today announced that the Committee will hold hearings on President Clinton's fiscal year 1996 budget proposals that are under the jurisdiction of the Committee. The Committee will receive testimony from Administration witnesses and the Director of the Congressional Budget Office. **The hearings will take place on Tuesday, February 7, Wednesday, February 8, and Thursday, February 9, 1995, in the main committee hearing room, 1100 Longworth House Office Building, beginning at 10:00 a.m.**

In view of the limited time available to hear witnesses, oral testimony at this hearing will be from Administration witnesses only. However, any individual or organization may submit a written statement for consideration by the Committee and for inclusion in the printed record of the hearing.

BACKGROUND:

On February 6, President Clinton will submit his fiscal year 1996 budget to the Congress. As previously mentioned in his State of the Union address, the President is proposing several tax initiatives. In addition, the welfare reform proposal advanced by the Administration affects several different areas of the budget, including Aid to Families with Dependent Children, which provides cash welfare payments to eligible beneficiaries and is solely within the jurisdiction of the Committee on Ways and Means. The Committee will also hear testimony on the general economic trends outlined in the budget and the spending, revenue and deficit projections in fiscal years 1996-2000. In addition, the Director of the Congressional Budget Office will present the economic and budget outlook as contained in CBO's February report.

In announcing the hearings, Chairman Archer stated: "In his State of the Union message, the President said he was interested in working with Congress in our effort to create a smaller, less costly government. The fiscal year 1996 budget will give us the details on how the President intends to achieve his policies, and ways in which we can work together to take government in the direction the public wants."

DETAILS FOR SUBMISSION OF WRITTEN COMMENTS:

Any person or organization wishing to submit a written statement for the printed record of the hearing should submit at least six (6) copies of their statement by the close of business, Friday, February 17, 1995, to Phillip D. Moseley, Chief of Staff, Committee on Ways and Means, U.S. House of Representatives, 1102 Longworth House Office Building, Washington, D.C. 20515. If those filing written statements wish to have their statements distributed to the press and interested public at the hearing, they may deliver 300 additional copies for this purpose to the Ways and Means Committee, room 1102 Longworth Building House Office Building, at least one hour before the hearing begins.

FORMATTING REQUIREMENTS:

Each statement presented for printing to the Committee by a witness, any written statement or exhibit submitted for the printed record or any written comments in response to a request for written comments must conform to the guidelines listed below. Any statement or exhibit not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

1. All statements and any accompanying exhibits for printing must be typed in single space on legal-size paper and may not exceed a total of 10 pages.

2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.

3. A witness appearing at a public hearing, or submitting a statement for the record of a public hearing, or submitting written comments in response to a published request for comments by the Committee, must include on his statement or submission a list of all clients, persons, or organizations on whose behalf the witness appears.

4. A supplemental sheet must accompany each statement listing the name, full address, a telephone number where the witness or the designated representative may be reached and a topical outline or summary of the comments and recommendations in the full statement. This supplemental sheet will not be included in the printed record.

The above restrictions and limitations apply only to material being submitted for printing. Statements and exhibits or supplementary material submitted solely for distribution to the Members, the press and the public during the course of a public hearing may be submitted in other forms.

Note: All Committee advisories and news releases are now available over the Internet at GOPHER.HOUSE.GOV, under 'HOUSE COMMITTEE INFORMATION'.

*****

NOTICE -- CHANGE IN TIME

ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

FOR IMMEDIATE RELEASE
February 2, 1995
No. FC-5-Revised

CONTACT: (202) 225-1721

TIME CHANGE FOR FULL COMMITTEE HEARING ON TUESDAY ON -PRESIDENT'S FISCAL YEAR 1996 BUDGET-

Congressman Bill Archer (R-TX), Chairman of the Committee on Ways and Means, today announced that the full Committee hearing on President Clinton's fiscal year 1996 budget proposals that are under the jurisdiction of the Committee previously scheduled for Tuesday, February 7, 1995, at 10:00 a.m., in the main Committee hearing room, 1100 Longworth House Office Building, **will begin instead at 10:30 a.m.**

All other details for the hearing remain the same. (See full Committee press release No. FC-5, dated January 30, 1995.)

******

Chairman ARCHER. Let me announce to the members of the committee that I am informed that Secretary Rubin is on his way over here from the Senate side. It is my intention to wait another 10 minutes, until 11 o'clock. He was due here at 10:30, and we are glad to accommodate the Secretary up to one-half hour. But at that point, I will recess the committee.

[Pause.]

Chairman ARCHER. I would like to ask all of our guests to take their seats so we can proceed with our hearing this morning.

Secretary Rubin, we welcome you to take a seat there at the witness table.

Secretary RUBIN. Thank you, Mr. Chairman.

Chairman ARCHER. We are pleased to welcome you to the committee. It is your first appearance here as Secretary.

Today is the first of 3 days of hearings on the President's budget. We will be hearing only from Secretary Rubin today. Tomorrow we will be hearing in the morning from the Secretary of HHS, Donna Shalala. Then we will finish this series of hearings on Thursday with the Director of OMB, Alice Rivlin, and the CBO Director, Robert Reischauer.

We have already completed our public hearings on the provisions of the Contract With America, hearing from a variety of witnesses, and today we are going to take time out from that schedule to listen to the administration and their views on the recently submitted budget.

Mr. Secretary, I can tell you from the start there are many things about this budget that we can agree on. You want to provide tax relief for the middle class, and so do we. You want to ensure that that is offset by spending reductions so that it is deficit neutral, and so do we. Very importantly, you want to make sure it is a policy that the Treasury can administer, and we agree with that.

In the end, it is the taxpayers who will judge our work, and there is nothing to be gained and everything to be lost by failing to work together. I am committed to working with the President and his Cabinet not only on tax relief but on welfare, health reform, and deficit reduction. I urge all of my colleagues to do the same and to start in a real spirit of cooperation by giving careful attention to the President's proposals.

Now for a brief opening statement, I yield to my friend, Sam Gibbons.

Mr. GIBBONS. Thank you.

Mr. Secretary, I think you can be very grateful to Chairman Archer for his courtesies. We are not usually this friendly to people who get stuck over in the House of Lords as long as you apparently did this morning. But I can think of other chairs of this committee who would have adjourned the meeting and said come see us in June or July.

I want to personally commend you, though, for the fine job that you have done in the administration. You are one of, if not, its principal adviser on economic policy, and I am pleased that the economy is in as good a shape as it is in. We are approaching full employment. We are approaching full use of industrial capacity. The business climate in general is considered to be very good in the United States as a whole.

This new budget moves in the right direction. It does reduce spending by $144 billion over a 5-year period. I think those figures are real. They are not phony. I commend you for that.

As I have said to you in the past, though, I really do not support talking about tax cuts now. I think it is the wrong economic thing to do. I know how it titillates every Member of Congress to be able to talk about tax cuts. It just makes us feel real good to be able to talk about that. But I think our emphasis should be, as painful as it is, on budget deficit reduction. I think that is the most important thing that this Congress and this administration should be doing.

I want to thank you and commend you again for the distinguished public career that you have had and what you have done for our economy, and I welcome you here. I hope this will be the first of many very informative discussions we have with you.

Chairman ARCHER. Without objection, any other opening statements by individual members of the committee may be inserted in writing in the record at this point.

[The opening statement of Mr. Ramstad follows:]

OPENING STATEMENT OF HON. JIM RAMSTAD

Mr. Chairman, I appreciate the opportunity to speak with Secretary Rubin about President Clinton's 1996 budget.

I must say I am disappointed in the President's newly released budget. President Clinton missed a golden opportunity for significant bipartisan deficit reduction.

Under the President's budget, the already massive budget deficit actually will increase over the next 2 years. While it's unfortunate the President has abandoned his campaign promise to halve the deficit by 1996, it's intolerable that this administration's deficits are increasing to such sky-high levels.

Unlike the President's budget, Republicans in the House will make a serious effort to control the growth of spending, which is driving up the deficit.

While I appreciate the administration's support for the Contract With America's family tax cut concept, the proposal to increase taxes on families once their children reach age 13 makes no sense. I've yet to hear one parent tell me that rearing teenagers is less expensive than rearing younger children.

Mr. Chairman, thanks again for calling this hearing. I look forward to hearing Secretary Rubin's testimony and to exploring in greater depth this important issue.

Chairman ARCHER. Mr. Secretary, again, welcome to the committee. We are pleased to receive your testimony, and you may proceed.

STATEMENT OF HON. ROBERT E. RUBIN, SECRETARY, U.S. DEPARTMENT OF THE TREASURY

Secretary RUBIN. Mr. Chairman, thank you very much.

First, let me apologize for being late, and thank you for your courtesy. I was, as you know, testifying at the Senate Budget Committee. While that had been arranged so that it would end in time to get me here on time, it turned out that that was not quite as easy to do once there as we had hoped it would be. So, again, I thank you for your courtesy, and I am very, very pleased to be here.

Chairman Archer, Representative Gibbons, members of the committee, I am very pleased to appear before you to present the President's budget for fiscal year 1966—1996, rather. [Laughter.]

Well, 1966 was an interesting year, too, but we are going to focus on 1996 in this particular budget.

Mr. GIBBONS. In 1966, the whole budget was $100 billion.

Secretary RUBIN. I actually remember 1966 fairly well. It was a good year. It was the year I started working, so I have some recollection of it. In any event, we will focus on 1996.

Let me say, Mr. Chairman, I am doing something that not many Treasury Secretaries get to do, which is to present a budget that continues a process of cutting begun at the start of this administration and that cuts taxes and increases public investments, both in ways designed to increase future productivity. That is the underlying philosophy of this budget: continuing the deficit reduction process and at the same time cutting taxes in ways that will help the middle class and at the same time provide incentives for saving, education, and other activity that will contribute to future productivity and also increase public investment.

OMB Director Rivlin will testify Thursday and provide details on the spending side of the budget. President Clinton, from the very beginning of this administration, has had a broad-based economic strategy to stimulate and then protect the recovery, to position the country for the long term, and to increase the incomes of working Americans. This strategy consists of fiscal discipline, private and public investment to increase long-run productivity, opening markets, reforming government and reforming regulation, and achieving health care and welfare reform.

The threshold issue we faced and the first issue that we dealt with when the President came into office was to bring the deficit under control after a long period of large and increasing deficits and at a time when we were facing projections for large and increasing deficits going forward. Working with Congress, we enacted a powerful deficit reduction program. As a result, the deficit has come down from $290 billion in 1992 to what we now project is $193 billion this year; or, to use a starker and, I think, more meaningful contrast, the deficit was on a track toward $400 billion in 1998 based on the programs that were in place at the end of the prior administration, and it is now projected, based on the deficit reduction that has been accomplished by this administration with Congress, to be $196 billion for that same year, 1998.

The deficit as a percentage of GDP, gross domestic product, goes from 4.9 percent in 1992 to a projected 2.7 percent for this year and a projected 2.11 percent of GDP in the year 2000, and we have a chart that shows that reduction.

I think, Mr. Chairman, and I think most observers of deficits in the economy believe that the most important measure of the deficit is the deficit as a percentage of the total income of the country, just as it would be for a private entity. How large is your borrowing relative to your income?

As our chart shows, we started with a deficit as a percentage of GDP at 4.9 percent. We wind up at the end of 10 years with the policies contained in this budget at 1.6 percent of GDP.

Fiscal discipline has been reestablished after a long period of ballooning deficits. The deficit has been reduced by more than one-half, both in absolute terms and as a percentage of GDP.

I worked in financial markets for 26 years, and I have absolutely no doubt that our aggressive deficit reduction program enacted by Congress was, in large measure, responsible for the decline in interest rates in 1993, which in turn was key to jump starting the economy in that same year.

Rates have now increased, reflecting growth, but the deficit premium, the critical impediment to growth, is in my judgment in very large measure gone. The increase in rates now is reflecting growth and is what you would expect to have.

We now have a strong investment-led recovery that is creating jobs. Business investment in machinery and equipment has increased dramatically and, as a percentage of GDP, is at an all-time high, as shown in the next chart. That is an enormous plus for future productivity.

The economy has created 5.7 million jobs, 5.3 million in the private sector. The unemployment rate has declined from 7.1 to 5.7 percent. With all the strength of the current recovery, the increases in the CPI, Consumer Price Index, still remain under 3 percent per annum for each of the last 3 years. This is an administration that is very focused on and watchful with respect to inflation.

In the long term, however, the success of our economy will depend on productivity growth. Productivity growth has been extremely slow for a generation, and this has contributed to slow growth in workers' incomes. Slow growth in average wages has been accompanied by an unequal distribution of income gains.

In the past 15 years, those with incomes in the lowest fifth of American households have seen their real incomes fall. Those in the top fifth have seen their real incomes rise, and the middle has stood still.

This budget emphasizes a three-part strategy to promote growth and improve the incomes of working Americans: one, maintaining fiscal discipline; two, providing tax relief for the middle class, tax relief that is targeted to also promote individual activity that will increase future productivity; and, three, increasing public investment in workers through education and training.

First, maintaining fiscal discipline. On a 10-year basis, as I mentioned a moment ago, our budget projects a reduction in the ratio of the deficit to the total economy, the deficit-GDP ratio, to 1.6 percent.

We continue reducing the deficit while lowering taxes at the same time by making substantial spending cuts in three areas. Restructuring government saves $26 billion, savings that come largely from five agencies—Transportation, Energy, Housing and Urban Development, the General Services Administration, and the Office of Personnel Management. We save $80 billion by further lowering the discretionary caps in 1996–98 and by extending the discretionary caps for 2 years beyond their scheduled expiration to the years 1999 and 2000. There is $32 billion in savings that comes primarily from the mandatory side of the budget through continuing some existing health care savings and various other items. A remaining $5 billion of deficit reduction comes primarily from lower debt service as a result of our success in lowering the deficit.

When you put all of these cuts together, they total $144 billion between 1996 and the year 2000. The President has proposed using $63 billion of these savings to provide tax relief to middle-income families as part of his Middle-Class Bill of Rights.

While the deficit is projected to continue to fall as a percentage of the economy for the next 10 years, eventually the deficit will turn up. The problems are an increasingly aging population and rapidly rising health care costs. If we want to maintain fiscal discipline over the long run, which our administration considers to be absolutely crucial, we must reform the health care system as soon as possible, and we look forward to working with Congress on that objective.

Before I leave our deficit reduction, let me make two additional points.

Under President Clinton—and chart 4 I think will show this—for the first time since the sixties, expenditures on government programs are less than the taxes paid by the American people. In other words, our deficit results from the burden of paying interest on the debt accumulated primarily by the deficits of the eighties.

The second general point I would like to make is that it is our belief, expressed many times in various forums, that the way to achieve deficit reduction is through deliberate and thoughtful policy choices, not through a balanced budget amendment.

Now let me turn to the question of providing tax relief for middle-income Americans.

On December 15, 1994, President Clinton announced his Middle-Class Bill of Rights. A middle-class tax cut has been an explicit goal of this President from the beginning. Many working American families have lagged behind, even in the past 2 years, despite our rapid rate of economic growth. Not only do these tax cuts provide immediate relief to middle-class families, but, very importantly, these tax cuts also serve a critical economic purpose by helping these families save and invest to become more productive and enjoy higher future standards of living.

We have targeted tax cuts squarely at the middle class. Eighty-six percent of the benefits of these proposals will go to families with incomes between $20,000 and $100,000. Let me briefly touch on the three components of the Middle-Class Bill of Rights.

First, the $500 child tax credit for children under 13. This credit is designed to help younger families, where economic pressure often tends to be greatest, to provide better child care, after-school activity, and the other requisites for good child rearing. This credit would reduce the Federal income tax burden of a typical two-child family with an income of $50,000 by almost 21 percent once the credit is fully phased in. This is an important investment in children, the future of our country.

Second, a $10,000 deduction for post-secondary education and training expenses. This deduction can be used by all members of the family, including spouses and children, and will help middle-income families better obtain the education and skills that will equip them to succeed at work in a modern economy. Again, people investing in themselves.

Third, expansion of individual retirement accounts. This program will substantially increase the availability of individual retirement accounts by raising the income ceiling to $100,000 for joint filers and $70,000 for individuals. Under the President's plan, the flexibility of the individual retirement accounts is greatly enhanced, which we believe will increase use and, thereby, savings. An individual can either deduct the amount deposited up front or forego this deduction in favor of tax-free withdrawal of all accumulated earnings after 5 years. Also, an individual may save for a broader range of purposes. Penalty-free withdrawals may be made at any time for specific purposes such as education, a first home, or certain medical expenses.

The point, Mr. Chairman, is to take the IRA and make it a more flexible savings instrument and thereby, hopefully, greatly increase its use and increase savings and the savings rate in this country, which will be a critical determinant of our future economic growth.

Finally, on the subject of taxes, one of the administration's priorities is to implement fully the Internal Revenue Service's Tax Systems Modernization plan to reduce the administrative burden on businesses and individuals and to raise compliance.

Public investing in the future: The President's public investment program, critical to future productivity, is many faceted. In this budget, it focuses on his GI bill for America's workers, which consolidates and streamlines a patchwork of some 70 job training programs to provide skill grants to lower income and displaced workers.

Mr. Chairman, to conclude, this budget is the next step in carrying forward the President's economic strategy designed to raise living standards for all Americans. A great deal has been accomplished in the last 2 years in putting in place the President's comprehensive economic strategy, and the results speak for themselves. But much remains to be done if this country is going to be effectively and properly positioned for long-term economic health. We enormously welcome the opportunity to work with you in the spirit that you expressed in your opening remarks on a bipartisan basis to continue moving forward.

Thank you, Mr. Chairman.

[The prepared statement and attachments follow:]

STATEMENT OF ROBERT E. RUBIN
SECRETARY OF THE TREASURY
BEFORE THE HOUSE WAYS AND MEANS COMMITTEE

Mr. Chairman and Members of the Committee:

I am pleased to appear before you today to present the President's proposed Budget for the 1996 Fiscal Year. I've been in office less than a month, but I am doing something not many Treasury Secretaries get to do: presenting a budget that cuts the deficit and cuts taxes. I am also doing something that you would have to go back 16 Treasury Secretaries to sometime in the Truman Administration to find: announcing that our budget deficit will decline for three years in a row.

As Treasury Secretary, my testimony will focus on broad policy issues and on the revenue proposals set forth in our budget. OMB Director Alice Rivlin will testify before you Thursday. She will provide greater detail on the program side.

Every Administration's agenda is contained in its proposed budgets. President Clinton, from the beginning of this Administration, has had a broad-based economic strategy to stimulate and then protect the recovery, to position the country for the long-term, and to increase the incomes of working Americans.

Prior to joining Treasury, I assisted the President in setting our overall policies. I know how deeply he feels about continuing to move forward on his full economic strategy, which includes fiscal discipline, boosting both private and public investment to increase long-run productivity, opening markets, reforming government and regulation, and achieving health care and welfare reform.

This morning, I would like to summarize briefly what we have achieved, where we are now, and where we are headed, with special attention to the President's proposed Middle-Class Bill of Rights.

What Have We Achieved to Date?

When the President came into office, the economy may have been in recovery, but the recovery was weak and uncertain. Employment growth, in particular, had lagged far behind normal expectations. Large federal budget deficits, which were increasing rapidly as a percent of GDP even as the economy was recovering, created an unstable economic environment. Escalating structural deficits were a clear signal that the chances of an eventual severe financial crisis were on the rise. Prudent business people were reluctant to hire or to invest in this unstable environment. As a result, Americans were experiencing a jobless recovery.

Thus, the first necessary economic move was to bring the deficit under control. Working with Congress, we enacted a powerful deficit reduction program. The $505 billion deficit reduction package was achieved largely through spending cuts of $255 billion over five years, including freezing discretionary spending at 1993 levels, and raising income tax rates on only the 1.2 percent of Americans with highest incomes.

We also introduced plans to reduce the size of government. The President's Reinventing Government initiative called for reducing the federal work force by 272,900 over five years, bringing government employment back to levels not seen since John Kennedy was President.

At the same time that we were cutting spending and government employment, we were able to reduce taxes for millions of lower- and moderate-income working individuals and families, and to offer tax relief for small businesses.

The net effect of our plan was to bring the deficit down: from $290 billion in 1992 to what we now project as $193 billion this year, the deficit as a share of GDP went from 4.9 percent in 1992 to a projected 2.7 percent for 1995.

I worked in financial markets for 26 years, and I have no doubt that our aggressive deficit reduction program was, in large measure, responsible for the decline in interest rates which in turn was key to jump-starting the economy in 1993. Deficit reduction also reduced uncertainty about our fiscal future and restored confidence conducive to investment.

In addition to addressing the deficit problem, we also made sure that American businesses had access to the credit they needed. When President Clinton took office, small- and medium-sized businesses were facing a "credit crunch." In response, President Clinton announced a program of regulatory and administrative changes to reduce impediments and increase the availability of credit.

The combination of these policies, a sound fiscal environment and increased availability of credit, has paid off. We now have a strong investment-led recovery that is creating jobs. The first chart at the end of this statement shows that business investment in equipment has increased dramatically under the Clinton Administration. As a percent of real GDP, business equipment investment is at an all-time high.

Most important, as we have cut the deficit and reduced federal employment, the economy has created 5.7 million jobs, putting an end to the jobless recovery. Note that 5.3 million, or 93 percent, of these jobs were created in the private-sector (see attached chart). At the same time, the unemployment rate has declined from 7.1 percent to 5.7 percent. Some say that all these new jobs are in low-paying industries, but that view is incorrect. Over the past year, the number of jobs in construction, which pays 30 percent more than the average wage, has surged by some 325,000. The decline in manufacturing jobs has turned around: factory employment is up 290,000. The high-paying wholesale trade and transportation and public utilities industries provided an additional 295,000 jobs.

All this investment and employment growth has occurred in an environment of low inflation--an absolutely critical objective of this Administration. Even with the strength of the current recovery, inflation has remained under control. The increase in the consumer price index has come in under 3.0 percent for each of the last three years. We see virtually no evidence of cost-push inflation pressure from wages. Growth of the employment cost index--the most reliable measure of labor costs--was lower in 1994 than it had been in 1993.

We have also established the basis for growth of future wages and living standards through our trade liberalization policies. We worked hard to enact NAFTA and GATT because we believe American workers will benefit. In an increasingly integrated world, we are going to have to look outward rather than inward if we are going to stay on top. Moreover, jobs in export industries are more productive than average and pay about 10 to 20 percent more than average. That means shifting the composition of GDP toward more exports automatically shifts the economy toward better paying jobs.

Where Are We Now?

As successful as economic performance has been in the last two years, getting the economy moving and creating jobs in the short term was only part of the challenge. In the longer run, the key test of this Administration will be whether it has succeeded in raising productivity growth--because that is the only way to create higher wages and higher standards of living.

I want to emphasize that productivity growth is not an academic abstraction. In the final analysis, increases in workers' incomes cannot be sustained without increases in productivity--in the amount produced per hour worked. Productivity growth has been extremely slow over the past twenty years. And slow productivity growth has meant slow growth in workers' incomes.

This slow growth in average wages has been accompanied by an unequal distribution of income gains. As you can see from the attached chart, in the past fifteen years, those with incomes in the lowest fifth of American households have seen their real incomes fall below the levels attained by their counterparts in 1980; those in the top fifth have seen their incomes rise by 21 percent; and the middle has stood still.

The unequal distribution of income gains over the past fifteen years has put very real pressures on middle-class families. Their standards of living have failed to match their legitimate expectations. Dealing with this problem is at the heart of the President's budget and his Middle-Class Bill of Rights.

Where Do We Go from Here?

This budget emphasizes a three part strategy to promote growth and improve middle-class incomes: 1) maintaining long-term fiscal discipline, 2) providing tax relief for the middle class, and 3) increasing investment in workers through education and training, as well as in machines and buildings. This is the approach that the President has outlined in his budget.

Maintaining Fiscal Discipline

This Administration fought hard to break the back of the cycle of ever-increasing deficits. But it is not enough to reduce the deficit for three years in a row. We are concerned both about the pattern of projected deficits over the next five years and also about the pattern after the turn of the century.

For the next five years, this budget maintains the progress on deficit reduction made in OBRA '93. As I said earlier, our projections show the budget deficit dropping in 1995 for the third straight year, this time to $193 billion. After 1995, the deficit, measured in dollar terms, fluctuates in a narrow range before falling back to $194 billion in 2000.

More important than stabilizing the deficit in dollar terms is reducing the deficit as a share of GDP. Between 1995 and 2000, the deficit-to-GDP ratio falls from 2.7 percent to 2.1 percent. We haven't seen numbers in that range since 1979.

Further, the attached chart shows that the deficit as a share of GDP has been cut in half from what was projected before passage of the 1993 deficit reduction package, fulfilling the President's promise.

This year, we continue our deficit reduction efforts and lower taxes by making substantial cuts in spending. Budget cuts come from three areas. Restructuring government saves about $26 billion. Most of that $26 billion is the result of fundamental changes in five agencies--the Departments of Transportation (DOT), Energy (DOE), and Housing and Urban Development (HUD), the General Services Administration (GSA), and the Office of Personnel Management (OPM). Additional efforts are aimed at terminating certain agencies and programs and restructuring others. In addition, we propose to turn over to the private sector or to state governments activities that they are well positioned to carry out themselves.

We have already had real success in this area. The President's reinventing government initiative has already reduced the federal work force by 102,500 positions. Currently, the federal work force as a share of total employment is at its lowest point since the 1930's. In addition, Congress has enacted $63 billion of the $108 billion in reinventing government savings proposed by the Administration. The goal is to make government even smaller and to make it work better for all Americans.

In addition, further lowering of discretionary spending caps from 1996 through 1998 and extending them for two years beyond their scheduled expiration in 1998 produces an additional $80 billion in savings. The budget contains specific proposals to achieve these savings. The net result of extending the caps and making the cuts will be to keep discretionary spending virtually constant in nominal dollars from 1996 through 2000.

Finally, $32 billion in savings comes primarily from the mandatory side of the budget through continuing some existing health care savings, imposing user fees for the lucrative electro-magnetic spectrum, accelerating student loan savings, and reducing certain agricultural programs. The remaining $5 billion of deficit reduction comes primarily from lower debt service, as a result of our success in lowering the deficit.

Together, our program cuts and projected debt service reductions save $144 billion between 1996 and 2000. The President has proposed using $63 billion of these savings to provide tax relief to middle-income families as part of his Middle-Class Bill of Rights. The remaining $81 billion is for deficit reduction.

If our proposed policies are continued beyond the year 2000, we now project that the fiscal year 2005 deficit will be only 1.6 percent of GDP. This good news comes from two developments. First, for the ten-year period from fiscal year 1995 to fiscal year 2005, the President's budget proposals produce substantial deficit reduction. Second, our new budget baseline projects lower spending for Medicare and Medicaid, based on the latest growth rate estimates from the actuaries at the Health Care Financing Administration.

Administration estimates of deficits in the out-years are noticeably lower than estimates that have been recently produced by the Congressional Budget Office. There are several reasons for this.

First, CBO's baseline, by convention, does not include any deficit reduction proposals. The President's budget proposes substantial deficit reduction over the next ten years.

Second, the Administration's baseline estimates include recent revisions to projected costs of Federal health care programs made by the actuaries at the Health Care Financing Administration. I do not believe that the latest CBO estimates incorporate the full revisions from the actuaries.

Third, over the long term, the Administration has a slightly more optimistic rate of growth for productivity--by one or two tenths of one-percent--than does CBO. By 2005, even very small differences in projected growth rates materially affect deficit projections.

In other words, there are straightforward explanations of the differences between our numbers and CBO's, and we are very comfortable with all our projections.

While we are confident that the deficit outlook for the next ten years is good, all observers agree that the deficit will eventually turn upward. The problems are an increasingly aging population and rapidly rising health care costs. We cannot do anything about the projected demographic shifts, but we need to do something about health care as soon as possible. If we want to maintain fiscal discipline over the long run, we must reform health care.

Before we leave our deficit discussion, let me make two additional points. First, let me refer you to an enlightening chart. This chart shows the difference between program expenditures and revenues for the Clinton Administration and for each of the last eight Administrations. Under President Clinton--for the first time since the 1960s--expenditures on government programs are less than the taxes paid by the American people. We have a deficit solely because of the burden of paying interest on the debt run up largely as a result of the deficits of the 1980s--not because we're overspending today.

The second general point I'd like to make is that I believe the way to achieve deficit reduction is through deliberate and thoughtful policy choices, not through a balanced budget amendment that greatly increases macroeconomic risk in our economy and involves spending cuts that have not been specified at the time the decision on a balanced budget amendment is made.

Providing Tax Relief for Middle-Income Americans

Let me now turn to the centerpiece of the President's budget. On December 15, 1994, President Clinton announced in an Oval Office address his "Middle-Class Bill of Rights." A major piece of his initiative is providing tax relief for middle-income families.

A middle-class tax cut has always been a goal of this Administration. In 1993, however, the Administration faced a deficit crisis larger than had been predicted at the start of 1992. Bringing the deficit under control, and directing tax relief to lower and moderate income Americans were our first priorities.

Due to strong, effective leadership and tough choices, the deficit reduction program has been even more of a success than expected. However, incomes of many working American families have lagged behind--even in the last two years, when growth in the economy has been brisk.

The President's tax cuts will not only provide immediate relief to financially-strapped middle-income families but also will help these families save and invest so that they will become more productive and enjoy higher future standards of living. Individual tax relief coupled with savings and investment will boost American productivity, providing the foundation for sustained increases in real incomes.

The Administration's tax cut is targeted squarely at middle-income families. The attached chart illustrates that a full 86 percent of the benefits of this tax cut will go to families with incomes between $20,000 and $100,000.

The tax cuts in the President's Middle-Class Bill of Rights have three elements, aimed at strengthening families, promoting education, and encouraging savings.

$500 Child Tax Credit: This credit is designed to help younger families, where economic pressure often tends to be greatest, to better provide child care, after-school activity, and the other requisites for good child rearing. This is an investment in children--the future of our country. A $500 (when fully phased in) non-refundable credit will be allowed for each dependent child under 13. Between 1996 and 1998, the maximum credit would be $300. This credit would reduce the federal income tax burden of a typical two-child family with an income of $50,000 by 21 percent. The credit will be phased out for taxpayers with initial Adjusted Gross Incomes (AGI) between $60,000 and $75,000. No credit will be available to taxpayers with AGI in excess of $75,000.

Deduction for Post-Secondary Education Expenses: This deduction can be used for education and training expenses for all members of the family, including spouses and children, and should better enable middle-income families to obtain the education and skills that will equip them to function effectively in a modern economy. This deduction is used in determining a taxpayers AGI (that is, taken above the line) and is, therefore, available to those who do not itemize their deductions as well as to those who do itemize. The maximum allowable deduction would be phased out ratably for taxpayers filing a joint filers with AGI (before the deduction) between $100,000 and $120,000 ($70,000-$90,000 for individuals). The maximum deduction would be $5,000 in 1996-1998 and $10,000 thereafter.

This proposed tax deduction of up to $10,000 in tuition and fees can be taken for study at any college, university, or vocational program eligible for federal assistance.

Expansion of Individual Retirement Accounts: This program will substantially increase the availability of individual retirement accounts by raising the income ceiling to $100,000 for joint filers and to $70,000 for individuals. Today, only couples with AGI up to $40,000 and individuals with AGI up to $25,000 can make fully deductible contributions. Moreover, the flexibility of the individual retirement account has been greatly enhanced: an individual can either deduct the amount deposited up front, or forego this deduction in favor of tax-free withdrawal of all accumulated earnings after five years. The President's proposal would allow penalty-free withdrawals immediately for specified purposes such as education, first homes, long-term unemployment, or certain medical expenses.

Other Revenue Proposals

In addition to the President's proposed middle-class tax cuts, the budget contains certain other provisions that affect revenues. An Appendix to my testimony provides further details. But let me note that we are proposing two additional empowerment zones, thus enlarging empowerment zone tax incentives; reducing a tax on vaccine manufacturers; denying the Earned Income Tax Credit (EITC) to undocumented workers, and to those with significant unearned income; changing the tax treatment of those who renounce their citizenship or use foreign trusts to shelter income; and supporting the extension of the taxes that finance the "Superfund" that cleans up hazardous waste sites.

Also, on the subject of taxes, one of the Administration's priorities is to fully implement the Internal Revenue Service's Tax Systems Modernization (TSM) plan to reduce the administrative burden on businesses and individuals and to raise compliance.

Investing for the Future

Fiscal discipline and middle class tax relief are necessary elements of any coherent economic strategy. Yet, by themselves, they are not enough to ensure higher standards of living for all Americans.

Additional investment in the skills and capabilities of America's workers and in physical capital have always been an integral part of the President's agenda. Today's investments will translate into stronger productivity growth and higher living standards for years to come. Boosting public investment is an important step towards a rising standard of living for all Americans.

Let me focus on three areas: investment in human capital; investment in science and technology; and investment in infrastructure.

Human Capital: The President has consistently emphasized the importance of "lifelong learning" in an economy which favors the highest skilled workers. The budget proposes $47.3 billion in 1996 for investment in education and training. This represents a $5.4 billion increase, or 13 percent, over 1993 levels. Working with Congress, the Administration has already launched legislation from expansion of the Head Start program to cutting the cost of higher-education loans for students.

This year, the President will focus on better opportunities for adults already in the work force. The President's proposal--the "G.I. Bill for America's Workers"--will consolidate and streamline a patchwork of some 70 job training programs. The "G.I. Bill" will offer dislocated and low-income workers "skill grants" through which they can make their own choices about the training they need to find new and better jobs.

Two other Presidential initiatives also deserve mention here.

Welfare reform fits into the over-arching strategy of raising economic growth. The current welfare system costs taxpayers a great deal of money and actually discourages work by participants. This Administration wants to work with Congress to make welfare a temporary safety net only, through time limits and through making work pay. If we succeed, we will both raise the standard of living of participants and lower the tax burden on average Americans.

Similarly, health care reform is not only essential to maintaining long-term fiscal stability, but also important for the take-home wages of the average American. If employees' health insurance costs keep rising, workers' wages won't. Health care cost containment will pay off in higher wages as well as in a more stable fiscal environment.

Science and Technology: We know that the rates of return for R&D are high in the private sector. Industry R&D may have accounted for as much as a quarter of overall productivity growth in recent decades. Commercial firms cannot reap the entire rewards of basic research, however, because other firms easily learn and use the knowledge generated. Despite high rates of return, the private sector does too little basic research to meet all of society's needs.

Thus, the federal government plays an important role in promoting and investing in R&D. Federal spending accounts for nearly 40 percent of the nation's R&D spending. This budget proposes $69.4 billion in 1996 for research and development--an increase of $3.74 billion in nondefense R&D over 1993.

Through the President's National Science and Technology Council, the Administration seeks to support the best possible science on a tight budget. The science and technology program pursues advances in health, business, the environment, information technology, national security, and basic science itself.

In addition, because of the importance of R&E to the nation's economy, we support the extension of the R&E tax credit on a revenue neutral basis, and we will work with Congress to pay for it.

Infrastructure: Infrastructure is one area where the government must play an important role--the private sector could not profitably run many of our nation's roads and bridges or the treatment plants needed to provide clean water. The budget proposes $58.8 billion for 1996 for infrastructure investment--up $8.6 billion from 1993.

While infrastructure spending can be among the most effective ways to boost productivity, projects must be chosen carefully. The Administration proposes to restructure the Transportation Department, consolidating its infrastructure activities into a single transportation block grant. Local governments will have more flexibility to direct resources to areas which best address community needs. Our goal is more and better infrastructure, at less cost and with less red tape.

Conclusion

In conclusion, let me make three points:

First, you can read the priorities of this Administration in its budget. This President is committed to raising standards of living for all Americans, and the policy objectives pursued through the budget--deficit reduction; the middle-class tax cuts; public investments in workers, in knowledge, and in infrastructure; Reinventing Government--are all aimed at attaining that goal.

Second, this budget maintains the ground won in the struggle to reduce the deficit in 1993. We project that, with the deficit-reduction policies in the budget, the federal deficit will remain below $200 billion in nine of the next ten years, and will shrink to 1.6 percent of GDP in fiscal 2005. We as a country simply cannot afford to return to the days of rising, uncontrolled deficits of the 1980s or early 1990s. This budget will keep us on a sound trajectory that reduces the deficit.

We do this by taking step-by-step reductions in spending programs and in cutting the size of government itself. Reinventing government not only saves money, but also makes government efficient. As a result of the Administration's actions to date, we are reducing the deficit and do not need a balanced budget amendment to enforce fiscal discipline. This is the right way to cut the deficit.

Third, we take a crucial step toward addressing the economic concerns of working families by cutting their taxes. Our proposals are targeted to the people who need them the most when they need them the most. These cuts will help families with young children, people who are paying for education, and those who want to save for the future.

This budget builds upon what has been achieved. It is the next step in the logical sequence of policies designed to raise the living standard for all Americans. It reinforces fiscal restraint. It provides tax relief to millions of Americans who have seen their incomes stagnate for a generation. And it invests in education, infrastructure, and technology.

Much has been accomplished in the past two years, but much remains to be done. I look forward to working with you on a bi-partisan basis to continue moving forward.

APPENDIX: OTHER REVENUE PROVISIONS

Additional Empowerment Zones. The Secretary of Housing and Urban Development would be authorized to designate two urban empowerment zones in addition to the six urban and three rural zones designated on December 21, 1994. This would have the effect of extending the empowerment zone tax incentives to these additional areas. Other current-law limitations, such as those regarding population, size, poverty, and application requirements, would be applicable to these areas.

Reduce Vaccine Excise Tax. Under current law, a manufacturer's tax is levied on vaccines used to prevent diphtheria, pertussis, tetanus, measles, mumps, rubella or polio. These taxes are deposited in the Vaccine Injury Compensation Trust Fund and provide a source of revenue to compensate individuals who sustain certain injuries or to families of individuals who die following administration of these vaccines. Because of large balances in the trust fund, the Administration proposes a reduction in revenues from these taxes. The decrease will allow continued program compensation while lowering the costs of vaccines to both public and private purchasers.

Earned Income Tax Credit

EITC denied to undocumented workers. Under this compliance proposal, only individuals who are authorized to work in the United States would be eligible for the earned income tax credit (EITC). When claiming the EITC, taxpayers would be required to provide a valid social security number for themselves, their spouses, and their qualifying children. Only social security numbers that are valid for employment purposes in the U.S. would enable the individual to claim the EITC. In addition, the proposal would modify the IRS procedure for processing returns with erroneous or missing taxpayer identification numbers so as to reduce improperly claimed credits. These proposals would be effective in 1996.

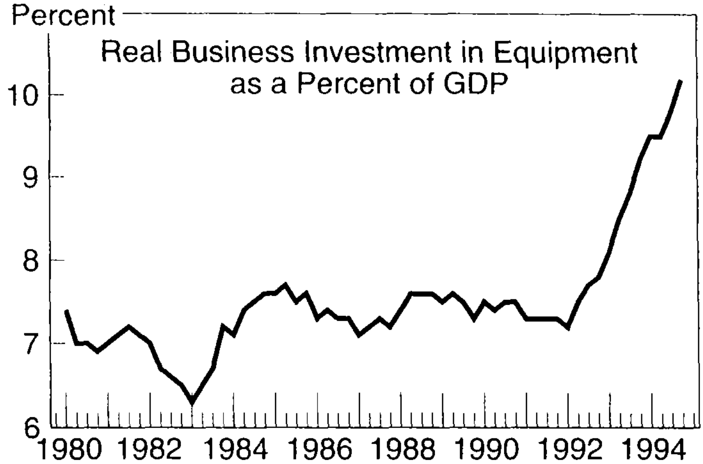
EITC denied if interest and dividends exceed $2,500. Under current law, an individual must have earned income in order to be eligible for the EITC. Because the EITC is designed to benefit low-income workers, the amount of the credit should decrease as the taxpayer's income increases. A taxpayer with relatively low earned income, however, may be eligible for the EITC even though he or she has significant interest and dividend income from investment assets. Under this proposal, taxpayers would not be eligible to receive the EITC if their combined interest and dividend income for the year exceeds $2,500. This proposal would be effective in 1996.

Tax responsibilities of Americans who renounce citizenship. The proposal would tax the untaxed gains of U.S. taxpayers who renounce citizenship. The tax would also apply to aliens who have been lawful permanent residents for at least ten years and then cease to be subject to U.S. tax. This tax is intended to apply only where very substantial gains are involved and, thus, an exemption is provided for up to $600,000 of gain. U.S. real estate and pension assets would also be exempt.

Foreign Trusts. The foreign trust proposal is designed to increase compliance for taxing two categories of people. First, U.S. persons sometimes transfer their assets to foreign trusts and rarely pay tax on the trust income. The proposal would impose enhanced information reporting requirements (with penalties for failure to comply) on U.S. persons who transfer assets to foreign trusts. The second category of taxpayers are U.S. persons who are members of wealthy foreign families. Foreign families often establish foreign trusts for the benefit of U.S. family members. Under current law, the United States treats such trust assets as owned by the foreign family, and any distribution of income earned by the trust to the U.S. beneficiary is treated as a nontaxable gift to the U.S. person. The proposal would tax this trust income.

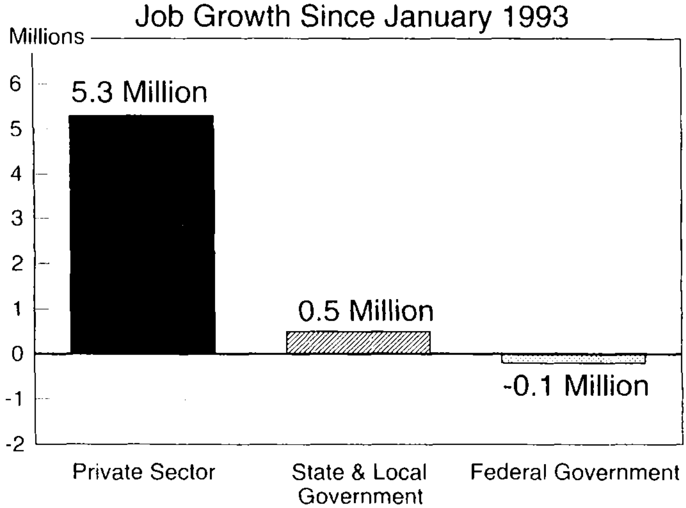
Extension of Superfund Tax. Four different taxes are imposed under present law to fund the Hazardous Substance Superfund (Superfund) program including a corporate environmental income tax equal to 0.12 percent of the amount of modified alternative minimum taxable income in excess of $2 million, and excise taxes on domestic or imported crude oil or refined products, certain hazardous chemicals, and certain imported substances. These taxes are scheduled to expire generally after December 31, 1995. The Administration supports the extension of the corporate environmental income tax through taxable years beginning before January 1, 2001, and the Superfund excise taxes through December 31, 2000.

Business Investment Has Surged



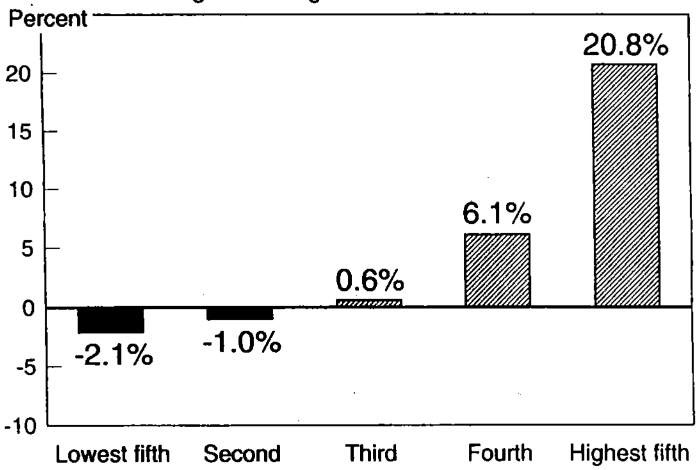
93 Percent of the 5.7 Million New Jobs Have Been in the Private Sector

Job Growth Since January 1993

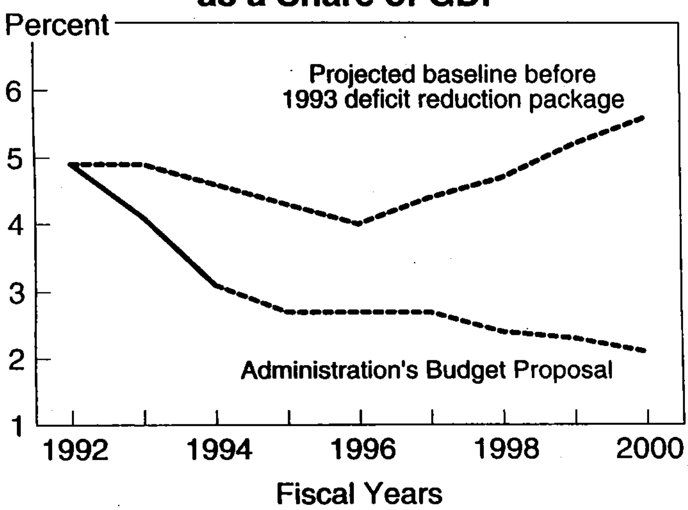


Middle Class Incomes Were Stagnant, 1980-93

Change in Average Real Household Income

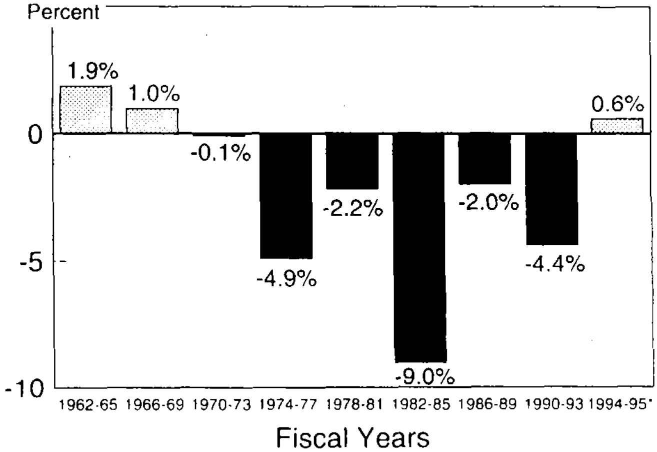


The Deficit Has Been Cut in Half as a Share of GDP



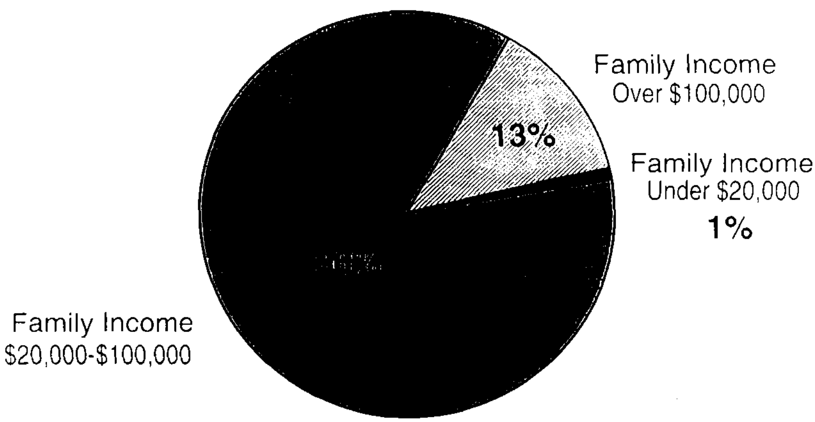
Spending on Government Programs Is Less than Taxes for the First Time Since the 1960's

Revenues Minus Program Spending as a Share of GDP



*Fiscal year 1994 and projection for fiscal year 1995.

Tax Cut Targeted to Middle-Income Families



Chairman ARCHER. Thank you, Mr. Secretary, and thank you for your very cogent testimony to the committee.

If I may ask you a question that is on the minds of average Americans that I have been hearing from, does the administration for which you work believe that we should have a balanced budget at the Federal level? That is simply a yes or no answer. You do not have to expound on it.

Secretary RUBIN. Let me express it, if I may, this way, Mr. Chairman, because I actually think it is a rather complicated question.

Chairman ARCHER. But it isn't complicated. Either we pay our bills currently or we don't, and the question is: Do you believe we should do that?

Secretary RUBIN. The President has said on many occasions that he believes that we should move toward a balanced budget, but we should do it in a careful and deliberate fashion and make sensible decisions each year that are appropriate in the context of the economic circumstances of that year.

Chairman ARCHER. OK. At what time does the President believe we should achieve the balanced budget?

Secretary RUBIN. The President believes very strongly, and I think rightly, that there should not be an arbitrary time; because once you have an arbitrary time, you have no way of knowing what the economic circumstances will be during your approach toward that arbitrary period, and you may be reducing the deficit at precisely the wrong time.

If, for example, we went into a recession and at the same time you continued to reduce the deficit, what you could do is turn a recession into something far more serious. That is really precisely the point. One should not have an arbitrary time. One should have a goal, and the goal should be to work toward a balanced budget in the context of the circumstances of every given year when the decisions have to be made.

Chairman ARCHER. Well, if the economy is doing as well as your charts say—and it is doing well based on what we hear from economists across the country—is not now the time when we should be able to pay our bills? We are not in a recession.

Secretary RUBIN. Mr. Chairman, it is our view—we would agree with you that this is a time when we should continue on the deficit reduction track. We began, as you well remember, in 1993. As I said in my opening statement, we inherited a situation that was viewed in the financial markets, and I think rightly so, as a fiscal morass, a fiscal mess. I think there was a prevailing sense of pessimism about fiscal order in this country. We put in place, with Congress, a very powerful deficit reduction program. This budget carries that program forward. Toward that end, we made $144 billion of cuts, and I will tell you, they came very painfully. If you do not believe me, ask the Secretaries who had to make those cuts.

We have used more than half of it for deficit reduction, and we have used some of it for tax cuts. That is what gets you on the path—well, the chart is not up there now, but that is what gets you on the path toward a 1.6-percent deficit-GDP ratio.

In our judgment, the next major step is to go at the item in the budget that really is driving the deficit, and that is health care expenditures.

Chairman ARCHER. But we still are not paying our bills this year, and we are at the height of a very successful economic recovery.

Secretary RUBIN. Mr. Chairman——

Chairman ARCHER. The American people, I think, have the right to ask: If we cannot pay our bills now, when will we pay our bills?

Secretary RUBIN. Mr. Chairman, I think your question is a good question. This is the kind of debate that we think should be undertaken with respect to economic policy. It is our judgment that you need to reduce the deficit in a powerful and aggressive but, nevertheless, a carefully balanced way. Because if you reduce it too rapidly, what you will do is have a negative macroeconomic effect on the economy, slow down growth, and possibly even push it into a recession. So it is for that reason that we have advocated being very focused on the deficit, but doing it appropriately over time.

Chairman ARCHER. But it seems to me the difficulty doing it over time is that as you project forward, most of your spending savings are going to be in outyears, that you may face the very thing you are talking about, which is an economy that is not as strong as it is now. The American people wonder why we are not doing more right now while we have a strong economy, and they also wonder, along the lines of your testimony, that the major problem in not getting to a balanced budget today is the interest charges for accumulated debt that was run up in previous administrations. Yet, as I understand your budget, you continue deficits year after year after year in your own projections of over $200 billion a year, which I believe you would agree is going to compound the debt and create more interest charges on future generations.

Secretary RUBIN. Mr. Chairman, conceptually, maybe the way to put it is this: What we have tried to do is design a program that will bring the deficit down as a percentage of the economy, very much as you would in looking at any sort of entity—how large is its borrowing relative to the size of its income?—and also begin to bring the debt down as a percentage of the total economy. That is what our program is designed to do.

It is our view that if you go too fast with respect to deficit reduction, you begin to run macroeconomic risks. On the other hand, we also believe that you should move as rapidly as you can because we agree with you that deficit reduction and getting the deficit down as a percentage of the total economy and getting the debt down as a percentage of the total economy are very important objectives for the long-term economic health of this country.

Now, we could have a debate—and it is a good, healthy debate—about exactly how rapid that process should be. I think we have done an enormous amount in the time that we have been in office, and we did it from the base of having inherited a very difficult and, I think, long-run untenable situation.

Chairman ARCHER. Well, I do not want to get back into who did what over the last 15 years, because we could be forever debating that, but we are where we are, and we have to move forward in a way that I believe tells the American people we are serious about getting to a balanced budget.

That is the one thing that troubles me about the budget you are submitting to us today. You are making projections over 10 years that still show deficits that do not go down but go up. If we cannot do it in a 10-year period, I think the American people can properly ask when. The answer is, if it is simply that we want the deficit to relate to the GDP growth rather than a balanced budget, I do not think the American people will buy it.

I may be wrong, but I have used up all my time, Mr. Secretary. So I am going to yield to my colleague, Sam Gibbons, for inquiry.

Mr. GIBBONS. Well, thank you, Mr. Chairman. I know the Secretary's time is limited. I know we are running late. The Secretary has been very generous with me in our discussions, and so I am going to yield back the balance of my time and let other people have a chance to question.

Chairman ARCHER. Mr. Crane.

Mr. CRANE. Thank you.

Mr. Secretary, since only one-third of married couples have children under age 13, and since the cost of bringing kids up escalates as they get older, I am curious why you came up with that cutoff age with respect to the tax credit for children at 13.

Secretary RUBIN. Mr. Crane, that is a good question. What we spent a lot of time doing was trying to figure out how to make our limited resources, because it is the President's view that every tax cut must be fully paid for and without any budget gimmicks, how do we make our limited resources most effective. The judgment that we reached was that it is younger families who have the most difficulty in terms of their incomes, and it is also young children who provide the greatest problem in terms of many kinds of expenses. I mentioned child care, after-school activity, and things of that sort.

So the idea was to focus the money on the people that we thought needed it the most and toward children at the age where we thought the greatest benefit could be obtained by enabling families to invest more in their uprearing.

I might add, incidentally, as kids get older and they get toward post-secondary school age, our education tax credit kicks in so that there is available help with respect to future training and schooling.

It is basically a question of targeting limited resources to the place where we thought it was most needed and would be most important to the future of our country in terms of investing in children.

Mr. CRANE. Another question is the education expense deduction which is limited to $5,000 in 1996, 1997, 1998, and then goes to $10,000.

What was the rationale behind postponing the elevation to $10,000 until 1999?

Secretary RUBIN. The President felt that an education and training tax deduction was a way to provide people with an incentive to do the things that will make them more productive, which is obviously good for the economy. Once again, you have the question of taking limited resources because he absolutely refused to have any tax cut that was not paid for; and, he wanted to accomplish deficit reduction at the same time that we had a tax cut. So we took our limited resources and we applied them in the manner that seemed most sensible, and to us that seemed to be to have 3 years of phase-in at $5,000 and then go to $10,000.

Mr. CRANE. A final question has to do with the proposal for border services user fees. I am curious as to why it is called a user fee.

Secretary RUBIN. It is called a user fee because it is going to be raised from people who legally, legitimately cross borders, and then the funds will be used predominantly for providing services to those people, for example, the border checkpoints and the various kinds of activities that Customs and others have to undertake to deal with legitimate crossings across borders.

Mr. CRANE. Well, frequent crossers are going to get a discount?

Secretary RUBIN. There is a frequent-crosser discount, yes.

Mr. CRANE. Aren't they using the border crossings like anybody else?

Secretary RUBIN. They are, yes, they are, and it is a good point. We actually discussed that. I think there was a balance struck, and the idea was that if people go back and forth a great deal, it would impose too much of a burden on those people. So the thought was to provide a discount, but that is a matter one could debate and have a different judgment on.

Mr. CRANE. I am just curious why it isn't referred to as a tax rather than a user fee, then, when you are making those kinds of arbitrary distinctions.

Secretary RUBIN. Oh, because I think that a user fee is a phrase in wide use to apply to a fee that is charged to people for a service that they are using as opposed to a general tax that is used for general purposes.

Mr. CRANE. These fees are designed to stem illegal border crossings and fight drug trafficking?

Secretary RUBIN. No. These fees are really designed to deal with the kinds of checkings and activities that are involved in legal, legitimate border crossings at both our northern and southern borders.

Mr. CRANE. They are not currently funded?

Secretary RUBIN. They are currently funded, but the idea here was to have them funded by the people who use the services.

Mr. CRANE. Thank you, Mr. Secretary.

Chairman ARCHER. Mr. Thomas.

Mr. THOMAS. Thank you very much.

Mr. Secretary, Sam Gibbons was very generous in the comments to you about this committee in the House versus committees in the Senate. I guess I would just ask you to go back and review article I, section 7 when you need help in terms of who is there constitutionally and what needs to be done.

We normally meet at 10 o'clock. We adjusted it to 10:30, and we basically waited until 11 o'clock. I would urge you to focus on the constitutional relationships.

In your statement, you talked about health care being significant in terms of controlling the deficit, and just prior to this, you mentioned that health reform or the failure to deal with health reform will drive the deficit.

What kind of health reform do you have in this budget?

Secretary RUBIN. Let me respond to both aspects of what you said, Mr. Thomas, because I agree with you. We had intended to be here at 10:30, and I do apologize for not being here. That was something that was unavoidable. But I do apologize.

Mr. THOMAS. Well, it is avoidable if you do not schedule it that way in the first place. So it is avoidable.

Secretary RUBIN. Well, let me apologize again. We did our best, and——

Mr. MCDERMOTT. Would the gentleman yield?

Secretary RUBIN. We are very pleased to be with you.

Mr. THOMAS. Thank you.

Mr. MCDERMOTT. Would the gentleman yield? I don't think you need to badger the witness when he was testifying in the Senate at the Senate Budget Committee.

Mr. THOMAS. I am suggesting, perhaps, that article I, section 7, that says that all revenue bills originate in the House of Representatives ought to enter into consideration of when you schedule committees, I would tell the gentleman from Washington, so that we don't get this dilemma that we have been presented with. That is all.

The gentleman will continue.

Secretary RUBIN. OK. In the spirit of being very pleased to be with you, let me respond to your health care question. [Laughter.]

Health care reform is not dealt with in the budget, and it is an extremely good question, and let me tell you why. We spent 2 years working on health care reform. We made an enormous and highly public effort to get health care reform. We did it because the President had the very strongly held view that, No. 1, all Americans should have health care coverage, and, No. 2, health care cost constraint was an absolute requisite for future economic growth.

We were unsuccessful in Congress. The judgment we made toward the end of last year and I guess the beginning of this year, but particularly toward the end of last year, was that in order to move forward toward the very same objectives that the President has advocated so vigorously over the last 2 years, what we should do is go through a different process, and that this time we should work with Congress in a partnership to try to accomplish these purposes.

When we sat down with the budget, it was our view that if we put a health care program in the budget, we would be getting ahead of Congress, and we would be undermining precisely what we were trying to accomplish.

Mr. THOMAS. Well, I appreciate the answer, but as you know, in 1993 the budget contained, in terms of the agreement, about a $56 billion cut in Medicare over 5 years. This budget contains about a $9.9 billion cut in Medicare, basically extending items to produce about a $65 billion cut over 7 years. You are quite right. The President's plan last year proposed a $124 billion cut in Medicare over 5 years.

In terms of your approaches in previous years, you focused on significant reductions in the Medicare program. In partnership with Congress, your choice now was to really offer nothing. Normally in partnerships you tend to work together to try to resolve problems. From my understanding of what you have said is that without a proposal from the President to reduce Medicare in this budget, it will force Congress to propose any changes?

So it is not a political document at all. You agree that we have to do something with Medicare, and reductions are part of the program. Is that what I understood you to say?

Secretary RUBIN. No. I think, Mr. Thomas, that my point was what we do in this budget is we extend some existing savings. We would not refer to those and I don't think they would be fairly characterized as Medicare cuts.

What I then said was that we believe very strongly that we need to move ahead on health care reform, we need to move ahead on reducing health care expenditures, but that the only way to do that, without having all sorts of adverse effects, is to do it in the context of health care reform. I think our last 2 years have proven that for us to get out ahead of Congress is not the way to accomplish health care reform——

Mr. THOMAS. I understand that——

Secretary RUBIN. —so we come to you with our hands out in partnership.

Mr. THOMAS. So that part of a plan which is a reduction in Medicare won't be used as a political tool to show that Congress wants to reduce Medicare and this administration does not, based upon your past offerings of significant reductions in Medicare. Is that correct?

Secretary RUBIN. No. I think that a more accurate characterization would be to say that we had last year a health care reform program in the context of which Federal health care expenditures would be brought down, enormous improvements and savings would be accomplished. That did not work, and we want to now go back and work with Congress on the question of health care reform to accomplish both universal coverage and cost containment.

Mr. THOMAS. Finally, then, even though you argue that health care reform is a necessity to help solve the deficit problem, you have offered no new ideas, not in partnership, but you are going to let Congress lead and you will follow.

Secretary RUBIN. No. I don't think that is an accurate characterization of where we are. We have put forward a budget which continues a powerful deficit reduction program begun in 1993——

Mr. THOMAS. No, no. On Medicare. On Medicare. My time has expired. On Medicare, do you have any ideas in the budget on Medicare?

Secretary RUBIN. I will get to health care. The percentage GDP figures were on the chart that now doesn't seem to be there. What we have said is we are not looking for Congress to lead. We are looking to work together with Congress. When we tried to lead, we led with our chin and we got socked. So the answer to that was let's not do that again, let's work in partnership with people for whom we have enormous respect, the Congress of the United States. That is what we are prepared to do.

Chairman ARCHER. The gentleman's time has expired.

Mr. Rangel.

Mr. RANGEL. Thank you, Mr. Chairman.

Mr. Secretary, it is difficult for us to give an analysis of your budget when we have absolutely nothing to work with, with the majority. I mean, they will be bringing us a balanced budget, and they will make certain that it is paid for by spending cuts. But we haven't the slightest idea where those cuts are coming from.

Now, it seems to me with this budget that you are saying that if you remove the payment of interest on our debt, then our spending would be less than the revenues we are raising.

Secretary RUBIN. That is right, Mr. Rangel. Had it not been for the interest on the debt, the vast preponderance of which was incurred during the eighties, we would be in a budget surplus position.

Mr. RANGEL. I think that everyone would admit that one of the most dramatic drives of our President and the administration has been to reduce the deficit that prior administrations have created.

Secretary RUBIN. I think that we have had an enormous accomplishment, beginning in 1993, in turning what I think could be fairly characterized as a fiscal mess into fiscal order.

Mr. RANGEL. So that when the administration decided to give a tax cut to middle-income families, it had to weigh that against continuing that policy of reducing the debt directly as opposed to a percentage of the——

Secretary RUBIN. No. There I would make a slightly different comment, if I may, Mr. Rangel. The judgment the President made was that there are many purposes that need to be achieved in an economic program if you are going to maximize economic growth and the wages of working Americans, and that the way to do that in this budget was to both continue the deficit reduction process and at the same time offer a tax cut.

Mr. RANGEL. Well, the tax cut costs about $63 billion.

Secretary RUBIN. Correct.

Mr. RANGEL. In the range of the people that would be the beneficiaries of it, do you have the average amount that a family will receive as a result of this middle-income family tax cut?

Secretary RUBIN. I don't, and in some measure it would depend, Mr. Rangel, on what they did. But I can tell you this: About 86 percent of the total tax cut package is aimed toward middle-income families, and I think—yes, we do have a chart that shows that. Families between $20,000 and $100,000 will receive——

Mr. RANGEL. That is a great breakout. But could you give me a guesstimate about what the average family will receive that is in the large size of that pie?

Secretary RUBIN. Well, I can tell you this: From the child tax credit alone, a typical family of four with an income of $50,000 will have their taxes decreased by about 20 percent. That is from that one tax credit. That is from one of the three components alone.

Mr. RANGEL. Well, I think that most of us who would prefer to have the deficit cut even deeper believe that the President's proposal on tax cuts is not going to have any direct impact on the economy, and it is not sufficient enough for the taxpayer to say thank you and that basically it is a campaign promise that he made and he wants to keep it.

Secretary RUBIN. No, I don't think I agree with that, Mr. Rangel. I think that for the families that avail themselves of these programs, I think that they will have a significant tax benefit. As I said, the child tax credit alone will be a 21-percent tax reduction for the average family of $50,000 with two kids.

But, more importantly, I think that what the President is doing is very important in terms of our future productivity and our future economic growth, because what he is doing is he is creating incentives for people to do things for themselves that will make them more productive and more effective in the modern economy.

It is really, I think, a very, very important set of incentives for people to do what is in their own interest and in the interest of the Nation.

Mr. RANGEL. Well, Mr. Secretary, I support the President's budget and want you to know that it is very easy for people like me to do this when we have this Contract With America hanging behind us. Thank you for your contribution.

Chairman ARCHER. Mr. Bunning.

Mr. BUNNING. Thank you, Mr. Chairman.

Secretary Rubin, there are so many questions, and I have so little time.

The budget for the current fiscal year is approximately $1.5 trillion. The President's proposal for spending is $1.612 trillion for fiscal 1996. The administration talks about the tough choices and how you had to make them to reduce the deficit.

Please explain to me and to the rest of the people how an increase of over $100 billion is a cut.

Secretary RUBIN. Mr. Bunning, I think you have to break the budget into pieces, and——

Mr. BUNNING. I do not want to do that. I want you to explain, answer the question.

Secretary RUBIN. I am in the process of explaining it, but I think to explain it, you have to break it into pieces.

On the discretionary side, we will have lower discretionary spending in each of the years of this budget than we had in 1995, which means not only is it lower in absolute terms, just absolute nominal terms, but if you adjust it for inflation, it obviously is a lot lower as time goes on; $100 today is not worth the same thing as what $100 will be 5 years from now. That was an enormously difficult accomplishment, and if you don't credit that, my suggestion, as I think I said before, is speak to the Secretaries who are now struggling with the need to accomplish what I have just said.

Now, spending keeps going up, because even if you get this piece under control—and getting this piece under control is a herculean task, and I think we have done an enormously effective job in doing it—you still have to deal with the question of health care expenditures. That gets us back to the very same point that Mr. Thomas and I were speaking about, and it is why I think the chairman's opening remarks are so welcome. It is absolutely essential that the administration and Congress join together to deal with Federal health care expenditures in the context of health care reform.

Mr. BUNNING. That is how you explain an increase of over $100 billion in spending, as a cut?

Secretary RUBIN. That is the analysis of our present budget situation. That is exactly right, Mr. Bunning. This is not a simple matter. The budget is a very complicated matter.

Mr. BUNNING. Sitting on the Budget Committee and sitting on this committee, we are very familiar with how tough it is going to be to get to 2002 and to balance the Federal budget, which we have made a commitment to do.

Let me ask you another question. If we run approximately $200 billion deficits in this range of 5 years—in other words, we are going to add $1 trillion to the debt—keeping in mind that the interest on the debt is approximately 16 percent of budget outlays presently, how long will it take for the interest on the debt to become the largest portion of our budget pie?

Secretary RUBIN. Actually, if we can stick with the deficit path that we outlined on the chart over here, where the deficit continues to fall as a percentage of GDP from the roughly 2.7 percent of our projection for the next year on down to 1.6 percent, what will happen is the debt will become a smaller and smaller percentage of GDP, and as a consequence, interest will become a smaller and smaller percent of GDP——

Mr. BUNNING. I didn't ask that question. I asked the question of how much—what percentage of the budget, not what percentage of GDP, what percentage of the Federal budget will be interest on the debt?

Secretary RUBIN. Well, if you can continue to bring the debt down as a percentage of GDP, then it seems to me over time what you will be able to do is start to bring interest down as a percentage of the total budget.

Mr. BUNNING. Doesn't it depend on how the interest rates are controlled and what interest rates we are paying?

Secretary RUBIN. Well, obviously, that comment assumes all other things being equal. Now, in terms of what interest rates are going to do—that is a very good point. In terms of what interest rates are going to do, if you stay on the path that we have suggested and if the deficit really does fall to 1.6 percent of GDP, I believe that you will have a very healthy interest rate environment.

I just came back from a G–7 finance ministers meeting this weekend in Toronto, and it was very interesting. We are viewed—and I think rightly so—as having gone from a fiscal morass to fiscal health.

Mr. BUNNING. I have one other question. I noticed in the budget that we just received there is no replacement for the $20 billion that the Federal Government has used out of the ESF, Exchange Stabilization Fund, to bail out the Mexican peso. Would that be something that you intended to do down the road? Or when are you going to charge off the $20 billion? We would like to hear the answer on that.

Secretary RUBIN. As we discussed, I think, in an earlier session, the Exchange Stabilization Fund is independent of the budget, and nothing that we are doing in Mexico, as a consequence, with the Exchange Stabilization Fund will result in any effect on the current budget.

Mr. BUNNING. In other words, you are not going to—you will not be required to replace that money?

Secretary RUBIN. The Exchange Stabilization Fund has been used with some frequency over time, and it has never had any budgetary effect. That is correct.

Mr. BUNNING. That is like our contribution to the IMF not having any effect, when it does.

Secretary RUBIN. Well, but once you have made the contribution to the IMF and it is in the IMF, then it does not affect the budget. Similarly here, what you have is a fund of money——

Mr. BUNNING. I asked a question about replacing the money.

Secretary RUBIN. We do not believe, Mr. Bunning, that what we are doing with respect to Mexico will create a situation in which we will be short of funds to accomplish the necessary purposes with respect to the dollar.

Let me say we were very, very, very careful, before proceeding with this proposal with regard to Mexico, to make sure that we had adequate funds in the ESF to continue doing what was necessary, if it does become necessary, with respect to the dollar.

Chairman ARCHER. The gentleman's time has expired. The chair is going to have to strictly use the time rules, because the Secretary, I believe, has to leave at 12:30. Is that correct?

Secretary RUBIN. It is, Mr. Chairman. But since I arrived a little bit late, what we are trying to do is postpone where we are going. We would really be very happy to stay with you.

Chairman ARCHER. I want as many members as possible to have the opportunity to inquire.

Mr. Jacobs.

Mr. JACOBS. Thank you, Mr. Chairman.

I want to begin with a public service announcement to all C–SPAN junkies. You probably heard the term "dynamic scoring," and it has just been discovered that Mae West, in one of her old movies, has defined that. She played the part of a teacher of elementary school children, and she took up math and said the following: "One and one is two. Two and two is four. Four and four is ten—if you know how to work it." So that explains dynamic scoring.

I want to say to the Secretary that I am one member——

Chairman ARCHER. Will the gentleman suspend for a moment? With all due respect to my good friend from Indiana, it is not in accordance with the House rules to speak to the television cameras or to the television audience, and I would ask all members hereafter to confine their remarks to the witness and to the members of the committee.

Mr. JACOBS. Thank you very much, Mr. Chairman. I withdraw the target and reincorporate my reference to the words. This is unfortunate because I was about to say that I am one member of the minority who agrees implicitly with our Republican chairman's questions concerning if not now, when, on balancing the budget. I have always believed that balancing the Federal budget would be about like the old Russian foreign trade policy: they exported the things they needed, and they imported the things they needed worse. If we would all give that some exercise, we might better define the distinction between need and want.

I have a nephew who has never wanted a Dairy Queen. He has always needed one. I think that we should all give some attention to that example.

In that spirit, Mr. Secretary, I only want to ask you about the child tax credit, whether it is the majority's or the administration's proposal. Does the Treasury Department have any calculations using the probability of—that may be dynamic scoring, too—the life span and the probability of the average income over that life span, how much each one of these children will end up paying in taxes, reflecting interest on the additional debt for the $500 credit for each one of them, depending on the age, 3, 5, 10, or whatever it is?

Secretary RUBIN. That is a very interesting question. The answer to your question is no, but analytically, that is a very interesting way to look at it. We have implicitly made a judgment. That is actually a very interesting way to frame that. We have implicitly made a judgment that the investment in the children today is worth more to those children than the savings that they would realize as a consequence of that much additional deficit reduction now over the course of their lives. That is how you framed the question. We have obviously implicitly made a judgment on that comparison of now and then, but we do not have numbers.

Mr. JACOBS. I understand.

Secretary RUBIN. But that is the right analytic framework, I think.

Mr. JACOBS. I understand your response and would accept it in the case of educationally disadvantaged children, where basic education is simply absent in the usually one-parent home and multichild home. I don't know that I could accept it in terms of people such as members of this committee. My wife and I have 5- and 3-year-old sons—the first time I was ever a father. No matter what our income is, we have a gift from God, the accident of having been born, each of us, in families where articulate English was spoken and where social grace was understood.

If you concentrated your help among those children who do not have that and, therefore, are condemned to a lifetime of ignorance because they cannot acquire the necessary linguistic skills, I would be applauding, even if the C–SPAN audience saw me doing it.

Secretary RUBIN. Mr. Jacobs, you actually, I think, would not qualify for our child care credit—not in any qualitative sense, but on an income basis, because we phase out——

Mr. JACOBS. I think that is true, but I did a little personal reference because somebody in my family, like my wife, might be watching this, and I just wanted to mention that. Probably not, Mr. Chairman, but maybe.

No, I am talking about the people who do qualify, obviously, for what you have proposed. I say if you would winnow the credit down to the children where it would make a difference in future income, then I would say that the credit is an investment and not, shall we say, a method of acquiring votes.

Chairman ARCHER. The gentleman's time has expired.

Mr. Houghton.

Mr. HOUGHTON. Thank you, Mr. Chairman.

Mr. Secretary, good to have you here. Mr. Secretary, just on a personal note, I came down here in January 1987, and I was convinced that it was sort of a stupid idea to have a law to defend you against yourself, because I thought we could balance the budget. But somehow we did not have the spine to do it, and so, therefore, reluctantly, I have joined the army of people who think that a balanced budget amendment is a good idea.

Now, I can understand your position that maybe a date certain isn't a magical figure. The thing that bothers me, however, is that the sustaining trends to get where we want to go—and this is incorporated in this year 2002—are not there. So we not only don't have a specific date, but we do not have a sustaining trend. According to your own testimony that what you expect is under a budget $200 billion in deficit of 9 of the next 10 years, that sort of bothers me. It is the trend that is important.

Secretary RUBIN. Mr. Houghton, we would agree with that analysis. I think where we would disagree, perhaps, is on the question of whether or not that trend is attainable without a balanced budget amendment.

Again, I would refer you to the chart that is on that easel. If the policy choices that we have made—and they are very tough policy choices—on the cutting of spending are implemented, then we will be on a path toward a balanced budget.

Now, if you add on top of that a program to deal with the entitlement that is really driving the deficit, which are the health care expenditures, I think that you will then find yourself on an even more effective deficit reduction path.

So I think it is within our ability to do this, and to do it without what we think are the very serious risks involved in a balanced budget amendment.

Mr. HOUGHTON. I know there are risks, and I think it is within our ability. But so far we really haven't been able to manifest that.

Since 1992, the last 2 years, the reason the deficit has gone down principally is because of the revenue increase, because, actually, spending has gone up during that period of time.

Secretary RUBIN. Well, I think you have really had two types of spending, and I think you have to look at them separately, Mr. Houghton. On the discretionary side, we really have gotten control of the budget, and that was an enormous accomplishment done at great cost. On the entitlement side, you are correct, and that is, once again, what drives us back to the need for health care reform.

I think if we are serious about the long-term deficit—and this administration, it seems to me, has manifested its seriousness at, in some ways, maybe great cost to itself. But we really have taken—I have said this before, but it is true—we have taken a fiscal morass and put ourselves in a position now where we are perceived, both in the markets and abroad, as being in a position of fiscal discipline.

If we are serious about going forward, I think we have to do two things: No. 1, go on the path on the discretionary side, which is outlined in this budget; and, No. 2, deal with health care reform.

Mr. HOUGHTON. Well, I think the fact that you are Secretary of the Treasury means an awful lot to the rest of the world. You create a great sense of leadership and stability.

However, when you take a look at what you said in terms of reducing spending, spending will not be reduced. If it is reduced, I don't see it in these figures, which, for 9 out of the 10 years, don't show any improvement.

Secretary RUBIN. Well, I don't mean to repeat myself, but spending on the entitlements side, you are right, has continued to go up, and it is going up at a rapid rate, and it will get worse because of demographics. It all drives us back to the same issue the President talked so much about in the last couple years—health care reform.

On the discretionary side, Mr. Houghton, I think we really have gotten this under control. We stabilize; we even bring it down some. At the same time, the economy is growing.

Mr. HOUGHTON. But, Mr. Secretary, the discretionary is only one part of it. Actually, it is one-third of the overall budget. Therefore, maybe a draconian move to have a date certain to force that trend line down in all spending is not such a bad idea.

Secretary RUBIN. Well, there I think is where the disagreement lies. It is our view that the hazards involved in an arbitrary date vastly exceed the benefits, and we think it far better and more sensible to engage in a deliberate and thoughtful process.

Mr. HOUGHTON. Thank you very much.

Chairman ARCHER. The gentleman's time has expired.

Mr. Shaw.

Mr. SHAW. Thank you, Mr. Chairman.

I would like to join my colleagues in welcoming you to this committee.

Secretary RUBIN. Thank you.

Mr. SHAW. In your testimony and according to your graph, you show that the deficit as a percentage of the GNP, gross national product, has gone down. I believe historically you will find that any year in which you have a substantial growth in gross national product because of increased revenue to the Federal Government and decreased expenditure in many programs, you will find that same phenomenon usually does exist in those particular years. Do you disagree with that?

Secretary RUBIN. Well, I think there have been times in the eighties where defense and other expenditures went up even though there was a growing economy. So I think actually that probably is—I would have to look back at the eighties, but I think that probably is not correct.

Mr. SHAW. Well, I——

Secretary RUBIN. I am not sure. We can look back at the eighties together at some point.

Mr. SHAW. I disagree with you, but a strong gross national product certainly favors revenue to the Federal Government, and it certainly favors decreased cost.

Secretary RUBIN. That is absolutely correct, and what this budget and I believe this administration has accomplished since we took office is to combine a period of economic growth with a period of real constraint on spending on the discretionary side. That is how we have accomplished the deficit reduction, and I think a very powerful deficit reduction, that has taken place and reversed the projections which really, I think, were quite alarming with respect to deficits that we inherited.

Mr. SHAW. In the area of welfare reform, how did you address that in the budget? I don't think that the President presently has a welfare reform bill. He had one last year. How did you handle that?

Secretary RUBIN. Welfare reform is not in the budget for the same reason that health care reform is not in the budget. It is a very complex area. It is an area on which we did put forth a bill last year. The bill was unsuccessful. The President made the judgment that the best way to proceed on welfare reform, which, as you know, has been a very high priority of his from the very beginning of this administration, is to work with Congress and, as the chairman said in his opening remarks, work with this committee to accomplish a very important purpose.

Toward that end, he had a conference a week or two ago—I have forgotten exactly when it was—to try to develop consensus around ideas in this area.

Mr. SHAW. Thank you. Thank you, Mr. Chairman.

Chairman ARCHER. Mrs. Kennelly.

Mrs. KENNELLY. Thank you, Mr. Chairman.

Mr. Secretary, as I travel around my district, one of the most attractive things that has been talked about this year is the tax deduction for education. Interestingly enough, I have been asked this question twice, and I thought it would be a good idea to ask you.

Evidently, the deduction is per family, not per child. It starts at $5,000 and eventually reaches a $10,000 deduction for tuition, not room and board.

Mr. Secretary, what happens if an individual has a family, divorces and has another family? This seems to happen. Evidently, this is a question in my district, so I am sure it is a question around the country. Would that individual be able to apply for two deductions, or would he have to allocate one?

Secretary RUBIN. That is an interesting question. Assistant Secretary Samuels, who is the Secretary for tax matters, says each family gets $10,000.

Mrs. KENNELLY. Well, that is going to relieve some people's minds. Thank you, Mr. Secretary.

Let me just go into another subject that I have had interest in over the years, and that is the EITC, earned income tax credit. I notice in the President's budget that he is suggesting that the Social Security numbers of those applying for the earned income tax credit be checked. Having been involved in this program for a number of years and having been very pleased when the President increased the EITC in his original budget, are we doublechecking this Social Security number because you found that we are dealing with fraud? If so, how much? Roughly, how much?

Secretary RUBIN. The President, as you know and as you said, has been a very strong advocate of the earned income tax credit, and it is part of this program of making sure that work pays for people as opposed to welfare. Really, in a sense, you could argue it is the first step in welfare reform.

The problem that we have run into—and the Treasury announced this some months ago; I have forgotten when it was—was that there is a fraud problem with respect to the EITC, and it is one that needs to be dealt with. What this program was designed to do was to be part of that process.

There is a process going on in Treasury right now to determine exactly what the specifics of the problem are, and at an appropriate time, we will have a public discussion of that. But I think at the present moment, probably the best thing to say is that we identified a problem, discussed it publicly, and this is part of the approach to dealing with that problem.

Mrs. KENNELLY. Well, I was pleased to see you doing this, because I think this is a very good program. It keeps people off welfare. It keeps them in the working world. So I am glad you are doing this.

Tomorrow we are going to mark up a small piece of legislation having to do with the individual deduction for health insurance for the self-employed. One of the ways we are looking at paying for it is another piece of your budget, and I find this very interesting. It is for people who get interest and dividends above $2,500 a year; they will no longer be eligible for the earned income tax credit.

Now, Mr. Rubin, granted, we do have fraud in certain areas. Granted, things happen. Everybody isn't up front about some things that they do. But may I ask you, what percentage—do we really have a problem with the earned income tax credit and $2,500 of interest and dividends?

Secretary RUBIN. Let me tell you what the theory is, and it is a good question. The theory is that the EITC really should be reserved for low-income people and that if they have assets sufficient to generate $2,500 of unearned income, then they ought not to qualify for it. It is a very, very small percentage. Don't hold me to this, but I think it is something like 2 percent of the total number of EITC recipients.

Mrs. KENNELLY. Well, I thank you for that answer. I was afraid almost to ask the question, because I really think this is a good program. You are trying to do the right thing by doublechecking the Social Security numbers, but I would hate to think tomorrow in the markup when we start talking about interest and dividend that we would think this is a serious problem. It is 2 percent of those claiming——

Secretary RUBIN. I believe that number is correct. Let me just check.

Yes, Secretary Samuels confirms that it is correct.

Mrs. KENNELLY. Well, I salute the administration for finding the 2 percent.

Thank you.

Secretary RUBIN. OK.

Chairman ARCHER. Mr. Herger.

Mr. HERGER. Thank you, Mr. Chairman.

Mr. Secretary, if you could tell me, is the goal of the President to come up with a balanced budget?

Secretary RUBIN. The President generally tends to express it this way. He believes very strongly in fiscal discipline, which is why we did what we did in 1993, perhaps at considerable political cost to himself, and that his objective going forward is to work toward a balanced budget, and that is the point we have been discussing a little bit here today, the chart that is still up there, plus the health care reform.

So the object is to work toward a balanced budget. I don't think there is any magic—I will speak for myself, but I know it is his view as well. There is no magic in exact balance. What there is enormous magic in is continuing to get the deficit down as a percentage of the total economy. That is the track we are on, and the next step is health care reform.

Mr. HERGER. The goal is not per se to come up with a balanced budget, but to work toward a balanced budget? I want to make sure I understand.

Secretary RUBIN. The goal is to have fiscal order, to continue to bring the deficit down as a percentage of GDP, and to work toward a balanced budget.

Mr. HERGER. Now, again, looking at the budget, it would appear that it is in the vicinity over the next 5 years of very close to $200 billion per year deficit spending. Is that correct, over the next 5 years?

Secretary RUBIN. What these projections show is that the deficit stays constant while GDP continues to increase, which, if you were running a private enterprise, is precisely what you would want to have happen so that your borrowing becomes a smaller and smaller and smaller percentage of your total income.

Now, if we can get health care reform effectively put in place, then you will see the deficit come down in absolute terms as well as a percentage of GDP.

Mr. HERGER. But in answer to my question, over the next 5 years the deficit will remain in the vicinity of $200 billion per year? That is what your numbers would indicate?

Secretary RUBIN. Yes, the percent——

Mr. HERGER. Which amounts to an additional $1 trillion, right, $1 trillion more debt in 5 years than we have now, which in turn is that much more interest on $1 trillion. Is that correct?

Secretary RUBIN. What you will find, as I said a moment ago, is that over the next 5 years the deficit in absolute terms stays, roughly speaking, constant while the economy continues to grow. Under those circumstances, I think what you will find is that the debt begins to come down as a percentage of GDP, which is a very healthy fiscal position for a country to be in.

Mr. HERGER. OK. That is not quite the question.

Secretary RUBIN. An enormous, just an enormous contrast to what happened during the eighties.

Mr. HERGER. But, yes or no, our debt will be increasing by almost $1 trillion over the next 5 years by your budget?

Secretary RUBIN. Well, my answer would be exactly the same as it just was, that we will have begun——

Mr. HERGER. The answer is yes; is that right? We will have $1 trillion more debt 5 years from now than we do now by the President's proposed budget, yes or no?

Secretary RUBIN. If we go ahead with the President's budget, which we obviously strongly believe we should, we will continue to address what we think is a very important problem, which is starting to get the debt down as a percentage of GDP, getting the deficit down as a percentage of GDP, and continuing the fiscal order in this country which is recognized both in international financial markets and in the international—what I call the community of international finance ministers.

Mr. HERGER. Well, those people I represent find it very difficult to understand how an additional $1 trillion debt over 5 years is working toward a balanced budget, as you mentioned was the goal, even though not a balanced budget but working toward it.

Let me move on to another question, again, that was alluded to in some previous questions. The concern we have is just how serious is the President? I have a concern that the President and the administration are not very serious at all. We were talking about discretionary spending. We have pretty well stated that we are not touching, we are not working on our entitlements, which is really the area that is escalating in the President's budget. I believe you did mention that we were working on discretionary spending. But isn't it true that the administration cuts in discretionary spending are really within the areas of defense and really not nondefense?

Secretary RUBIN. We have a total discretionary budget. It consists of defense and nondefense. Defense goes down somewhat, and the nondefense piece goes up somewhat. But the fact is that if you put the two together on the discretionary line, what we have done is presented a budget where discretionary stays below the 1995 level for 5 years in a row. I would guess—and I don't know this because I haven't done this—that you would have a very, very hard time finding an equivalent period back a long way in American history.

Now our challenge is to get a hold of health care entitlements, and the way to do that is in the context of health care reform.

We can do this. We have presented a budget which really provides a way to continue moving dramatically toward a balanced budget if we could just add to our budget the health care reform effort.

Mr. HERGER. Well, I am not sure if you answered the questions I asked, but, anyway, I do thank you.

Chairman ARCHER. The gentleman's time has expired.

I couldn't help but think, Mr. Secretary, as you struggle with trying to answer these balanced budget questions, that, in fact, you are saying we will get to a balanced budget all in good time, all in good time, but not in my lifetime.

Secretary RUBIN. Well, could I characterize it a little bit differently?

Chairman ARCHER. Well, you have already couched it, I think, several times.

Secretary RUBIN. I have already done it. OK.

Chairman ARCHER. Mr. McCrery will inquire.

Mr. MCCRERY. Thank you, Mr. Chairman.

Mr. Secretary, you seem, at least to me, to be sending conflicting signals somewhat. On the one hand, you say we have a great budget here, and we ought to stick to it. Then on the other hand, you say, but we do need health care reform and welfare reform. You don't really want to stick with this budget for 5 years, do you?

Secretary RUBIN. What we would like to do is stick with this budget for 5 years, and then add to it two more programs: one, health care reform, and the other, welfare reform.

Mr. MCCRERY. OK. So you don't really want to stick with this budget. You want to have this budget, and then you want to do health care reform and welfare reform to bring the deficit down further. Is that correct?

Secretary RUBIN. Well, you can use the words "stick with" any way you want, but we believe very strongly that this budget is a multifaceted response to the very complex problems of our economy. It gets us on a good path with respect to the deficit, and now we want to do two more things, the two that you have just mentioned.

Mr. MCCRERY. Right. So you would like to do more than is in the budget that you are presenting us today over the next 5 years?

Secretary RUBIN. Yes. We have a very ambitious attitude toward economic issues; therefore, we have an ambitious budget, and, therefore, we have the ambition of going further with respect to health care and welfare reform.

Mr. MCCRERY. Well, I am glad that you have got that straight, because we want to do more than is in the President's budget to get toward a balanced budget. Some of us want to get to a balanced budget.

The bottom line is, though, you surely agree that we cannot achieve a balanced budget or even get close to a balanced budget unless we reduce the growth of the Medicare program and the Medicaid program.

Secretary RUBIN. It is the President's expressed view, which he has talked about enormously in the last 2 years, that health care expenditures, Federal health care expenditures, have to be dealt with, but in the context of health care reform.

Mr. MCCRERY. Thank you.

Some of us are concerned—and maybe you can put me at greater ease than I am, but some of us are concerned that our vision into the future stops short of a real problem. When we are talking 5 years or even 10 years, we are not really looking at the long-term economic health of this country, because around the year 2015, 2016, 2017, we are going to have a dramatic turnaround in the income and outgo of the Social Security system.

It seems to me that if we don't get to a balanced budget some time fairly soon, and maybe even run a little surplus to buy back some of the publicly held debt to put us in a better position, financial position to deal with that turnaround in the second decade of the 21st century, then we are going to be depending on the rest of the world, basically, to finance our needs. That would put us in a not very desirable position.

Do you disagree with that assessment?

Secretary RUBIN. Well, the President is very much focused on the long term. There was a very interesting article about 1 year ago in the New York Times that said a lot of the things the President is doing, and doing at tremendous political cost to himself, are things that will not pay off until well after his 8 years in office.

On the question of Social Security specifically, the projection, if I remember correctly, is exactly what you said. Somewhere around 2015 or thereabouts the balance changes, and then by 2030 you really run into the problem of not having enough funds. Clearly, that is an issue—although it is well off in time—that is going to have to be dealt with at some point.

It is our view, and I think rightly, that that is going to have to be dealt with on a bipartisan basis after extensive public debate. It is, however, a fair bit out in time, and our suggestion would be that the much more immediate question on the entitlement side is health care and health care reform, which is why the President took the enormous political risk he took last year in that arena.

Mr. MCCRERY. Well, I was not talking about changing Social Security, although that is something future Congresses can address. We are all agreed we are not going to touch Social Security, so leave that aside. I am just talking about the economic consequences of the turnaround in the trust fund. Right now we are using $60 or $70 billion a year from the trust fund to pay for ongoing operations of Government, to put it simply. Around the year 2015, 2016 or so, that is not going to be available to us, and, in fact, we are going to be paying out more from the Social Security trust fund than we are paying in.

We are going to have trust fund balances sufficient to pay those, but, still, the operational side of government is not going to be in as nearly good a position as it is even today with our deficit.

Secretary RUBIN. Which is precisely why we feel—and I have a feeling we maybe share a view on this—that we have got to continue to get this deficit down and get to work on health care reform and do it as quickly as possible.

Mr. MCCRERY. Well, I agree, and I commend you for your efforts. I just hope that you will work with us to go further faster, because some of us think that if we don't do something soon, we are going to create an even bigger problem very early in the next century. We need to do something more dramatic than you propose in the next 5 years.

Secretary RUBIN. Let me say in the spirit of the chairman's opening remarks, we are very much looking forward to working with this committee on the whole range of issues that really are going to affect the future of this country.

Mr. MCCRERY. Thank you.

Chairman ARCHER. Mr. Levin.

Mr. LEVIN. Thank you, Mr. Chairman.

Someone said earlier that there was no spine in this institution. I think you have reason to have some pride in what was done the last years, and there were some with spines here. Something was done. But now sinners are preachers around here.

Let me ask you, in terms of percentage of GDP, it was 5.4 percent in 1985, a time of relative prosperity, reduced to 2.7 percent now, and projected to be 2.1 percent.

In 1 minute—pretend you are on television—explain to——

Secretary RUBIN. I am not allowed to do that.

Mr. LEVIN. I said "pretend."

Secretary RUBIN. Oh, pretend. OK.

Mr. LEVIN. Explain the significance of percentage of GDP represented by the debt. Really, in 1 minute, try to say it simply, because it is said that you cannot get that across.

Secretary RUBIN. To put it in maybe the simplest terms that I can think of, at least, if you have an individual with an income of

$100,000 and that individual borrows $1,000, that is a very prudent thing. It will not interfere with other activities the individual wants to undertake, and it doesn't in any way threaten the financial future of the individual.

If a person with an income of $5,000 borrows $1,000, they are in a horrendously different position, and I think that is probably an analogy that maybe is helpful when you think about the country as a whole.

Mr. LEVIN. Now let me ask you a question that manifests my concern about the level of the debt. I want to ask you a pointed question. The tax cut represents about $15 billion on the average in the next years. It also goes up the last years, like every other tax cut proposed around here. So, again, briefly, why is it more important to spend that $15 billion a year in a middle-class—that is the middle-class tax part of it—rather than reserving that or allocating it specifically for this vital goal of deficit reduction?

Secretary RUBIN. Mr. Levin, I think that is exactly the kind of policy debate that we should have in this country as we look at this budget. It was the President's judgment, I think very rightly, that the additional $63 billion of deficit reduction would have less beneficial impact than would a program that would have some offsetting effect on the declining real wages that too many middle-income Americans have had, and very importantly, that would give people incentive to save and to invest in themselves, their children, in education, and training. So the judgment is: Which of those two programs is better for this economy over the long run? The judgment he made was that the system of incentives and tax decreases that we put in place is the better use of that money. But that is a very good public debate to have.

Mr. LEVIN. Better for the middle-class families that the tax cut is aimed at, right? You can even narrow it down. For the typical middle-class taxpayer, which is better: to use that $15 billion—I use that because it goes up each year—for middle-class tax relief or to reduce the deficit? For the typical family in my district, that becomes the issue with the importance that is given to deficit reduction. In 1994, I proudly said I helped to reduce the rate of increase in the deficit. Now I have got to answer the question: Which is more important for these middle-income families?

Secretary RUBIN. I think what I would recommend, at least, or suggest is that the philosophy of this budget is we are doing both. We are continuing the process of deficit reduction that began in 1993, and we are also making a judgment with respect to the $63 billion that you are talking about, that for middle-income families, they over time will become more productive and benefit more economically and, therefore, the Nation will benefit more economically by spending the money in the way that we are on these incentives for education, for training, for child care and so forth, than by an addition to the deficit reduction of that amount of money.

Mr. LEVIN. Thank you.

Chairman ARCHER. Mr. Hancock.

Mr. HANCOCK. Thank you, Mr. Chairman.

The President's budget has a projected 5.5-percent increase for this next fiscal year. The projection for GDP increase is what?

Secretary RUBIN. For which year are you talking about now?

Mr. HANCOCK. For this next fiscal year.

Secretary RUBIN. For 1996 we are projecting a 2.5-percent increase in real gross domestic product.

Mr. HANCOCK. A 2.5-percent increase in GDP and a 5.5-percent increase in the budget. It seems to me that a few years ago there was an effort started here on the Hill to control the increase rather than looking at GDP and what have you, but to control the increase to around 4 percent. In fact, I think it was called the 4-percent solution, then the 2-percent solution.

My question to you, Mr. Secretary, is: How can we continue—I mean, regardless of what we do, if we project the gross domestic product to increase 2.5 percent, and then we submit a 5.5-percent increase in the budget—I mean, we cannot keep doing that.

Secretary RUBIN. Well, what we need to do—and I believe this budget does do it, and that really was the purpose of this chart, to show that if you implement a budget that is designed the way this budget is, it will get at exactly the question you are raising, which is bringing the deficit down as a percentage of GDP—in nominal terms. So if you are stating that is your objective, we would be in absolute agreement with that.

Mr. HANCOCK. But I still think that we need—are going to have to take bigger steps in this next fiscal year's budget than what has been presented. I think some way we have to get it back in line with the people's ability to pay. That is why some of us supported on the balanced budget amendment a percentage limit of GDP as an expense, as part of the balanced budget amendment.

Secretary RUBIN. You used a very interesting expression, and it is probably one I should have used in response to Mr. Levin's question. It is ability to pay that maybe explains best why deficit as a percentage of GDP is really, I think, the most economically sensible way to look at the deficit. Your ability to pay for any given amount of deficit, or if you are an individual, any given amount of personal debt, is obviously greater the greater your income. So what we have tried to do—not tried, I believe what we have done is to put in place a budget which will continue to bring down this deficit-GDP ratio; in other words, continue to improve the ability of the Nation to pay for the deficit in any given year.

Mr. HANCOCK. The fact remains that people pay the total cost of government. That comes out of personal income. That is the only place it can come from. Yet we don't really have any studies on that because we don't have any figures on what total personal income is less Government transfer payments. Government transfer payments build up the totals of personal income, but we don't even know for sure what those figures are. That is one of the things that I would like to see us in some way start looking at.

Secretary RUBIN. Well, I think we can give you in writing a submission on personal income and transfer payments. I think we can actually be of some help to you in that respect.

Mr. HANCOCK. I would like to have that information.

Thank you, Mr. Chairman.

[The following was subsequently received:]

The attached table provides detail on the composition of personal income for the latest three years. The great bulk of the transfer payment component of personal income represents transfer payments by government, both Federal and state and local. Such government transfer payments represented 16.5 percent of total personal income in 1994.

The figures are taken from the National Income and Product Accounts for the United States. The figures are printed in various issues of the Survey of Current Business published by the Commerce Department.

COMPOSITION OF PERSONAL INCOME IN RECENT YEARS

	Billions of dollars			Percent of Total		
	1992	1993	1994	1992	1993	1994
Personal income total	$5,154.3	$5,375.1	$5,701.7	100.0	100.0	100.0
Wage and salary disbursements	2,974.8	3,080.8	3,279.0	57.7	57.3	57.5
Other labor income	328.7	355.3	381.0	6.4	6.6	6.7
Proprietors' income with inventory valuation and capital consumption adjustments	418.7	441.6	473.7	8.1	8.2	8.3
Rental income of persons with capital consumption adjustment	(5.5)	24.1	27.7	(0.1)	0.4	0.5
Personal dividend income	161.0	181.3	194.3	3.1	3.4	3.4
Personal interest income	665.2	637.9	664.0	12.9	11.9	11.6
Transfer payments to persons	860.2	915.4	963.4	16.7	17.0	16.9
Old-age, survivors, disability, and health insurance benefits	414.0	444.4	473.5	8.0	8.3	8.3
Unemployment insurance benefits	38.9	33.9	23.3	0.8	0.6	0.4
Veterans benefits	19.3	20.1	20.1	0.4	0.4	0.4
Government employees retirement benefits	109.9	118.7	126.9	2.1	2.2	2.2
Other transfer payments						
Aid to families with dependent children	23.3	23.9	24.2	0.5	0.4	0.4
Other	254.9	274.4	295.3	4.9	5.1	5.2
Less: Personal contributions for social insurance	248.7	261.3	281.4	4.8	4.9	4.9
Addendum						
Government transfer payments to persons	837.8	892.6	939.9	16.3	16.6	16.5
Total personal income less government transfers	4,316.5	4,482.5	4,761.8	83.7	83.4	83.5

Source: National Income and Product Accounts of the United States

Chairman ARCHER. Mr. Ramstad.

Mr. RAMSTAD. Thank you, Mr. Chairman.

Secretary Rubin, good to have you here today at the hearing. I think former Democratic Senator Paul Tsongas enjoys widespread bipartisan support, certainly in this body, as he does across the country. I think he put it best in commenting on the budget when he talked about the annual deficits of nearly $200 billion yearly for the rest of the decade in the budget. He said, "It is obvious the Clinton administration gave up the ghost on a balanced budget." I continue the quote of Senator Tsongas, "That is a pretty devastating fact of life."

I think that is pretty devastating for people where I come from. I know it is very devastating for people where I come from, and I think it is very, very unfortunate that there isn't an attempt to balance the budget. I think if anything derived from the message of November 8, the election, was that people want us to get our fiscal house in order.

For 26 years—and certainly there is enough blame to go around, historically—but for 26 years, since 1969, we have not had a balanced budget from the Federal Government. I think it is a national outrage. Then you come up and say we will get to a balanced budget all in good time. You are quoted today in the Washington Post as saying you do not want to have an arbitrary time by which the budget has to be in balance.

Well, Mr. Secretary, with all respect, it seems to me the American people want and deserve a balanced budget, and it seems to me a greater effort should be made.

Having said that, by your own Office of Management and Budget figures, the debt will increase from $5 to $6 trillion, which is an increase of 20 percent, by the end of 1996. If I heard your testimony correctly today, you said the debt will go down as a percentage of GDP.

Well, do you actually think that GDP will go up by more than 20 percent, therefore?

Secretary RUBIN. No, but as long as you have the deficits—let me go back to the first thing you said, though, because I think it is very important, with respect to Mr. Tsongas.

With all due respect to Mr. Tsongàs, I don't think there is any question—we agree with you. The American people want their fiscal house in order, and I don't think that there is any question but that this President in the first 2 years of his administration has manifested an enormous commitment to fiscal order. In fact, I could make the argument that it was the enormous commitment to fiscal order and the things that we did to reverse what really had been a fiscal morass that may have cost a fair bit politically.

Having said that, we are now on the right road, and this budget is designed toward keeping us on the right road and getting this budget down in the manner that I described.

Mr. RAMSTAD. What year will we see a balanced budget pursuant to this plan?

Secretary RUBIN. I think it would be a very serious error of economic policy to have an arbitrary date for a balanced budget for the reason that I said. I don't think that you can feel any more strongly than I do about fiscal order. But I think that the issue that we are debating—and it is a good debate—should you have an arbitrary date, with all of the economic rigidities that that creates, including loss of the automatic stabilizers, the risk that I first became very troubled about when somebody first talked to me about a balanced budget amendment, which is trying to squeeze into a preset arbitrary period all the reduction that you would need to take place to reach the balanced budget, when you did not know what the economic circumstances were going to be like.

So I think that the hazards, the macroeconomic hazards, the economic hazards, the risk of creating slow growth or even recession by working toward an arbitrary date make that a very unsound economic policy. I think what is a sound objective is the one that I think you and I would agree on, which is fiscal order and continuing to move toward a balanced budget.

Mr. RAMSTAD. Well, Mr. Secretary, with all respect—and I do have a lot of respect for your expertise and your experience, your background and your education, you would certainly qualify as an expert witness were we in a legal proceeding. Therefore, I could ask you the question: Would you speculate, would you guess that it would happen in our lifetime? I think we are about the same age.

Secretary RUBIN. I think I feel somewhat older—not as a consequence of this proceeding, just my last 2 years—I think my speculation would be as follows, that we have a President who is enormously committed to fiscal order and that we will continue to move on this track as aggressively as makes economic sense, and particularly so if we can work together toward the common objective of health care reform.

Mr. RAMSTAD. Again, Mr. Secretary, with all respect, I think your response underscores the need for the balanced budget amendment. We have heard this line for 26 years in this country, and again historically there is enough blame to go around on both sides of the aisle, and we understand that. However, that was then and now is now. We have got to balance the budget, and I just hope the amendment passes.

Thank you.

Chairman ARCHER. Mr. Secretary, we are going to take a break now and go to vote, and hopefully that will give you some time to stretch your legs and loosen up your back and relax a little bit. We will be returning after the vote, as soon as we can get back.

Let me simply say before we do leave, though, that I have a real problem with your analogy of a family whose income is going up and, therefore, it is OK to borrow more each year. You increase your debt because your income is going up, and as long as your income is going up more than the increase in your debt, everything is OK.

The problem is that in the real world things do not go up forever, and when a correction occurs, you are left with this tremendous mountain of debt. Debt which you said it is OK to keep increasing as long as you do not increase it as much as your increase in earnings. Then you are left high and dry with the inability to be able to service that debt when times are lean. I am concerned that we as a country are a combination of families where things will not go up automatically all the time, and that we had better start thinking about taking our increase in earning capacity and reducing our debt, rather than continuing to see it go up.

If you want to respond in 30 seconds, I will go and vote.

Secretary RUBIN. My 30-second response, Mr. Chairman, is that we would share your objectives. I think the difference may be in how we get there and how we balance those objectives against other objectives. But we would share your objectives.

Chairman ARCHER. The committee will stand in recess.

[Recess.]

Mr. ZIMMER [presiding]. Could you please be seated. I have been instructed by the chairman to get started without him, in the interest of time.

Secretary Rubin, you have said a number of times today that the principal reason why the deficit numbers start tailing up again in the outyears is because of the problem of health care, and that if we enact health care reform, that will be the way to bring the deficit down toward zero.

Are you aware of the fact that the CBO, Congressional Budget Office, in the last Congress calculated that if the Clinton health care plan were enacted, it would in fact increase the deficit rather than reduce it?

Secretary RUBIN. We submitted a comprehensive health care plan, and what you said is correct. When they scored it or evaluated what it would cost, they said it would increase the deficit. It was not our judgment, but our response to that was that we would reconfigure it so that we would accomplish deficit reduction, and we in fact did do that so that we would have a plan that would accomplish deficit reduction.

Having said that, the brief I was making was not for the plan that we put forth last year, although I think that plan was structurally very sensible. But that is neither here nor there. It was not a brief for that plan. It was a brief for working with Congress to accomplish health care reform.

Mr. ZIMMER. Do you have any idea on how we can reform health care in a way that actually reduces, rather than increases, the deficit, and how that would differ from the plan that was originally scored by CBO?

Secretary RUBIN. We have had a process going for quite some time in the administration focusing on the question of health care reform. We have a lot of thoughts that we think are worth pursuing with Congress. It was our view, and I think rightly, that the way to do this is really to work cooperatively with Congress, not get out ahead of Congress. I think the appropriate thing to do is to engage in this structure with the members of this committee and others who are involved with health care and work these out together, rather than my coming out and putting forth proposals once again, or ideas which could once again interfere with that process.

Mr. ZIMMER. Mr. Secretary, I would suggest that you not rely so heavily on health care reform as the reason why the budget cannot be balanced, if the one specific plan that was put forward by the President would have increased the deficit, and if the administration is not prepared to submit another one.

Secretary RUBIN. Mr. Zimmer, I think that the plan that we put forth, I think it would have resulted in deficit reduction, particularly in the outyears when health care entitlements start to increase. In its first iteration when we first put it forth, you are absolutely correct in your observation. The Congressional Budget Office disagreed with us on some numbers. What we did then was to reconfigure the plan so that we would accomplish even by their standards deficit reduction in the outyears. But that was all for naught, because it did not get adopted in Congress.

Mr. ZIMMER. I would like to follow up on a question that Mr. Ramstad put to you about whether in fact the national debt is going to decrease as a percentage of GDP as a result of your program. As he summarized it, the debt is going to go up by 20 percent in 5 years. In order for it to be a lower percentage of the GDP, the GDP would have to go up at least more than 20 percent. How do you account for that?

Secretary RUBIN. I should have responded. I apologize. We got caught up in another subject, and I apologize for not responding.

The debt, as you say, would increase by something in the neighborhood of 20 percent. GDP in that period, if GDP grows at the rate we projected, which is a real increase of 2.5 percent—and that, as you know, is after adjustment for inflation—that comes out to about, if you have an inflation rate of 3 percent, which is roughly what we are projecting, that would give you 5.5 percent per annum, so that is 27.5 percent over a 5-year period.

I apologize for not responding when he asked the question.

Mr. ZIMMER. Thank you.

One final issue. We have debated in this room and elsewhere what the eighties really meant and what lessons can be learned from it. It seems to me we are now starting a similar debate about the nineties. You have said that it was the interest rate reductions that took place during the Clinton administration that accounted for the economic recovery. What was the interest rate on the long bond when President Clinton was sworn into office?

Secretary RUBIN. The interest rate on the long bond, that is 30-year government, was roughly 7.7 percent, which is roughly where it is today.

Mr. ZIMMER. What was it 1 year before that?

Secretary RUBIN. I can describe what happened. I do not remember the precise rate, but I will tell you what I at least think happened, and I spent 26 years running very, very large trading operations, so it is something I know a touch about.

I think what you saw happen was interest rates come down, long-term rates come down, rather, during the years of the prior administration, because we were wallowing in what was effectively a virtually no-growth or very low-growth economy. I think what happened is they came down to about as low as they would have gone, and we still had a very large deficit premium in long-term rates.

Then the Clinton administration began working on a deficit reduction program and that started to get into the public domain, not through our release really so much, as to some extent through leaks and some extent through I guess some discussions as to what we were doing. The markets believed for the first time in a long time there was going to be discipline with respect to the deficit, and then rates came down to something under 6 percent in 1993, and they then came back up. When they came back up, it was not because they had a deficit premium. It was because we were growing, and so the 7-percent rate you have today is a very, very different interest rate than you had in the end of the last administration.

Mr. ZIMMER. But was not the economy growing fairly rapidly at the end of 1992?

Secretary RUBIN. Well, what actually happened is you had a fairly good first quarter, you had two quite poor quarters, and then the fourth quarter was strong. But it is very interesting, if you look at the fourth quarter and break it down, what you find is that the first month was not particularly good, and the second 2 months were very good.

The other interesting thing is that the consumer confidence index jumped remarkably in the last 2 months, and I believe that what happened is that there was this general sense of morass and slow growth and lack of fiscal discipline and all the rest that was burdening the economy, and that with the election of the President, there was a sense of change and that in turn, as evidenced by the consumer confidence index, improved the general mood and that in turn fed into the economy.

Mr. ZIMMER. So the bottom line is that when interest rates go down, even when they go down in somebody else's administration, it is because of Bill Clinton. But when they go up, it is not?

Secretary RUBIN. No, I think the bottom line is that you need to look not only at what interest rates are doing, but why they are doing it, and that is what people in markets spend their lives doing is trying to figure out not only just very simply what the rate is doing, but why did it do it. In this case, I think what you had was the restoration of a sense of fiscal discipline and that caused rates to go down, and now they have come back up with growth.

Mr. ZIMMER. Well, if you had a budget that you proposed to us with a plan for getting to a balanced budget by the year 2002, do you believe that would reduce interest rates as a result?

Secretary RUBIN. Well, I think that would depend on a lot of circumstances. But I think if we did what you just hypothesized, I do not think that you would get—this is my view—I do not think that the macroeconomic impact of trying to compress all of that deficit reduction into a preset arbitrary period is worth the risk that it exposes the economy to. Obviously, to the extent that you have the deficit going down and you have a negative macroeconomic impact, that can get offset by lower interest rates.

My judgment, for whatever it is worth, is that the lower interest rates would not generate enough activity to offset the negative impact of arbitrarily getting down to a balanced budget by 2002 under many circumstances that you hypothesize. So I do not think it is worth taking the risk of being arbitrary. I think we should do it year by year.

Mr. ZIMMER. Regardless of whether it is worth taking the risk, you do think that it probably would reduce interest rates?

Secretary RUBIN. Oh, if we had a recession, it would reduce interest rates. But the object is to get interest rates down by virtue of fiscal discipline, not by virtue of slowing down the economy or, even worse, having a recession.

Mr. ZIMMER. Thank you very much.

Mr. Kleczka.

Mr. KLECZKA. No questions.

Mr. PAYNE. Thank you very much, Mr. Chairman.

I noticed as you were making the presentation and looking at these charts that the deficit has been reduced 3 years in a row, which is the first time since Harry Truman was President that we are able to say that. I also noticed that, as a share of GDP, the chart that is being shown now, that the budget has been cut in half since 1992, again the budget deficit as a percent of GNP.

My recollection, as I was thinking about my time on the Budget Committee in the 102d Congress when Mr. Darman came and talked to us about OMB and projections at that time, the last projection I remember seeing for the years 1997 and 1998 were that we would have a budget deficit that would be close to $400 billion. Would you comment on that as the starting point from which you and the administration began this process?

Secretary RUBIN. Mr. Payne, your recollections are correct. We were in Washington in December 1992 during the transition, and I guess in early January, and beginning to prepare the President-elect's economic program, and we had a sense of what we would try to accomplish, how we would balance one thing against another. Then the last numbers of the prior administration came out and I remember calling the President-elect—he was in Little Rock at the time—and saying the projections are far worse than anybody expected and it looks to us as if they amount to a $400 billion deficit in 1998.

His reaction was our first priority has to be to get our fiscal house in order. If we are now facing those kinds of deficit prospects, we have to have a plan that is correspondingly effective on deficit reduction. The result is the program that we began in 1993 will continue in this budget—and we will take that same year you just mentioned, Mr. Payne, 1998—and instead of having a $400 billion deficit, the one that was projected based on the last numbers of the prior administration, we have a projected deficit of roughly $193 billion or less than half of the previously projected number.

Mr. PAYNE. I think we can look at a lot of progress, and I was one of those who participated in the 1993 deficit reduction package. I think certainly that could be pointed to as one of the things that has happened that in fact allowed us to be able to say today for the third year in a row, we reduced the budget deficit.

I am also one of those who has sponsored the balanced budget amendment and feel that we need to work toward balancing the budget by a date certain, in the year 2002. As we have held hearings on the Contract With America, I have been concerned about some of the projections that we have seen relative to some of the cost of the elements of the contract. I believe the Joint Tax Committee has just come out with some estimates that say the cost will be roughly $200 billion over 5 years and $700 billion over 10 years. Do your own numbers confirm that?

Secretary RUBIN. Mr. Payne, as part of our responsibility to deal with issues of tax policy, we evaluated the Contract With America when the tax proposal was first put forward, and our judgment on the 10-year numbers was something like—I think it was a little over $700 billion. I have forgotten the exact number, $720 billion or some such number, and we were criticized for having arrived at such a number.

We now have observed that the Joint Tax Committee has come up with approximately the same number, a shade over $700 billion. Yes, our numbers which originally were criticized by some turn out to be almost the same as the Joint Tax Committee. Both are estimating that the Contract With America tax provisions will cost a little over $700 billion over a 10-year period.

Mr. PAYNE. In the budget we are looking at today, over a 5-year period, middle-income tax cuts savings provisions amount to roughly $63 billion. If we had the provisions of the Contract With America in lieu of these provisions, that number would not be $63 billion, but, rather, $200 billion and, consequently, we would need to find another $137 billion in additional cuts in order to be at the same place that your budget is as it relates to the deficits in the outyears. Is that a correct assumption?

Secretary RUBIN. Yes, the answer to the question, Mr. Payne, is that accords with our numbers. Of course, it raises the question, since we all seem to agree that the President certainly said this, and I think there is general agreement, that all tax cuts have to be fully paid for and without using unusual budgetary practices, how this is going to get paid for. How ours is going to get paid for is very clear. It is in the budget. We have specific budget cuts.

Mr. PAYNE. So the task we will be faced with on this committee is looking at many of these provisions, many of which are very desirable, but in the light of knowing that we will have to find an additional $137 billion in cuts over and above the President's budget in order to stay at precisely the same place?

Secretary RUBIN. Well, that is to stay in the same place. But if you also want to accomplish deficit reduction, as we thought was imperative and as we did, of course, then you have to find considerably more than the amount that you have just mentioned.

Mr. PAYNE. Thank you very much, Mr. Secretary.

Mr. ZIMMER. Mr. Johnson.

Mr. JOHNSON. Thank you, Mr. Chairman.

Mr. Secretary, you kind of used the words "deficit" and "debt" interchangeably.

Secretary RUBIN. I do not believe I did. They are obviously very different concepts.

Mr. JOHNSON. We talk about the debt going up in precise dollar numbers. How much is it going to go up in your budget?

Secretary RUBIN. Under our budget, as I think I discussed before with—I have forgotten which member it was now——

Mr. JOHNSON. I do not think you ever answered him.

Secretary RUBIN. What I said was that under our budget it will begin, not to go too far, but we will begin for the first time in a long, long time to get the debt down as a percentage of the total economy.

Mr. JOHNSON. As a percentage, but what is the exact number? It has gone up over $1 trillion, to be truthful, has it not?

Secretary RUBIN. It will go up in absolute terms, but if I may say so, Mr. Johnson, if you as an individual or if you were a business entity looking at your debt, I think what you would look at is how well is it covered, in other words, how large is it relative to your ability to service it. The answer to that question in the context of a nation is what is your debt relative to your GDP.

Mr. JOHNSON. I think you would find in business that people are going into bankruptcy, chapter 11, trying to figure out how to get out of the position that we have got ourselves. We are not doing that. We are not even addressing the problem.

Secretary RUBIN. I know a fair bit about business. My instinct would be to think that if we were a business, we would be enormously critical of what we did in the eighties and what we would be trying to do now is just continue to get our debt down as a percentage of our total income.

Mr. JOHNSON. You also spoke about health care being a problem. I do not think the numbers are there to indicate that health care by itself, to quote a Perot phrase, "will fix itself." So what else do you propose to bring the debt and deficit down?

Secretary RUBIN. Well, if you were to adopt the program that we put forward, then, as the budget book shows, you get the deficit down by the year 2005 to 1.6 percent of GDP. The only items in the budget that are of major consequence that are growing faster than the rate of inflation are the health care expenditures, so I do think that is the area that we should be focusing on. If we can accomplish something there, you can really get yourself in the position that many of you all believe in and that we believe in, which is to get an even more rapid rate of decrease in the deficit as a percentage of the total economy.

Mr. JOHNSON. It surprises me that you all did not discuss that at all.

Also, you talk about, well I think you called it wallowing in fiscal discipline—causing the interest rates to do what you described. Does that mean you do not have fiscal discipline now?

Secretary RUBIN. No. What I said was that in my view rates came down in the early nineties because of a broad-based feeling that we were not only wallowing in a period of very slow growth, which we were, but that that was likely to continue for a long time.

I think what happened in very early 1993 is that the financial markets began to see a seriousness about fiscal discipline they had not seen in a long time, and that then took the deficit premium largely, not totally, I do not think, but largely out of long-term rates, so then rates started to go down again, but for a different reason. Now rates have come back up, but they have come back up reflecting growth, which is what you want. What you want is a system where the deficit premium is largely out of long-term rates. Rates go up when you are growing fast, they go down when you are growing more slowly, and then you have a system that works.

Mr. JOHNSON. Do you see it slowing down right now?

Secretary RUBIN. It is our projection and judgment that the economy will grow at something like 2.4 or 2.5 percent over each of the next 2 years, and that, as you know, is——

Mr. JOHNSON. For the long term, and you expect interest rates to continue up?

Secretary RUBIN. Well, let me say what our projection is on interest rates. Our projection on long-term interest rates is that interest rates this year in 1995 will average 7.9 percent. Given the rates are below that now, I suspect in a fiscal sense that may turn out to be a conservative assumption, and then we assume rates will come down to about 7 or 7.1 percent on the long side.

Mr. JOHNSON. Thank you very much, sir.

Thank you, Mr. Chairman.

Mr. ENGLISH [presiding]. Thank you.

Mr. Secretary, I have a couple of brief questions. First, with regard to the extension of the R&E tax credit, which I believe in your testimony you indicated the administration would be receptive to, with the qualifier that it be revenue neutral. I applaud your willingness to go on record in support of the extension. My question for you is can you offer us any detail in how you might be prepared to pay for it?

Secretary RUBIN. Our view on the R&E tax credit, which, as you know, the President has been in favor of all through his administration——

Mr. ENGLISH. I understand.

Secretary RUBIN. —is that it is a tax credit that has bipartisan support, and what we need to do is sit down with the members of this committee and the Senate Finance Committee, but I guess primarily this committee in the first instance, and determine how to pay for it, much as we did with GATT last year. As you may remember, there was broad-based bipartisan support for GATT. The question was how to pay for it, and we sat down with the relevant committees and worked out a way to pay for it.

Mr. ENGLISH. We have discovered in the course of our hearings on tax policy that there is some consensus among the experts that because of our tax structure in this country as it applies to business, particularly as it is imposed on our manufacturing sector, you can make a very powerful argument that our workers are put at a competitive disadvantage with respect to many of the other workers in countries across the globe who are laboring in different tax climates. Do you share that view, Mr. Secretary?

Secretary RUBIN. I think rather than answer it in that most general sense, tell me a little more specifically what you have in mind.

Mr. ENGLISH. I was actually looking for generality. A couple of people that we have had testify have suggested that, taken as a whole, given the tax structure as it is imposed on—let us take manufacturing, to be specific—that our workers in those industries are at a competitive disadvantage because of the tax structure.

Secretary RUBIN. My instinct would be to think not. A study was released recently—and I think it was McKinsey, but do not hold me to that, but I think it was, which is a very highly respected consulting firm—that reported that, for the first time in a long time, our industry was the most competitive in the entire world, so that——

Mr. ENGLISH. That would be based on quite a few factors.

Secretary RUBIN. Yes, it would be based on many factors, I absolutely agree with that.

Mr. ENGLISH. My own view, and I suspect my experience is considerably less than yours, is that American workers are at some kind of a competitive disadvantage. I noted in your testimony, and I want to applaud you on this, that you take considerable credit for the administration for the fact that business investment has increased and that there is an increased investment specifically in machines and buildings. I think those sorts of investments protect the jobs of American workers in a dynamic and increasingly competitive international marketplace.

The question I am moving toward is would the administration, provided it would be deficit neutral, be supportive of some additional tax incentive for investment in capital equipment, whether it be neutral cost recovery—and we have heard testimony from the administration expressing some concerns on the design of that tax credit—or some other similar tax break? Again, assuming it does not balloon the deficit, could the administration be supportive of that kind of tax benefit?

Secretary RUBIN. A neutral cost recovery proposal, which we have looked at and analyzed, in our view, and my view personally, has an enormous cost and it seems to me exceedingly unlikely to produce benefits commensurate with the costs. Beyond that, it is hard for me to comment on something in quite that hypothetical a stage, but we would be happy to discuss any proposal that comes from members of this committee, if those are proposals that are designed to be helpful to the economy.

Mr. ENGLISH. Do you feel it should be a priority of the committee to consider an affordable tax break to encourage capital investment, specifically in manufacturing and, shall we say, specifically in smaller manufacturers?

Secretary RUBIN. I think the best thing that this committee can do in terms of investing in manufacturing is to continue on a path of fiscal discipline, because, as that chart shows, investment in equipment and machinery—it was not buildings, by the way, it was equipment and machinery—is at an all-time high.

So I think we need to keep on the deficit track that we have put ourselves on or at least that this budget would put us on. We did in fact in the 1993 budget put forth expensing for small business, and it is something the President very much favors. I suspect that if there was a desire to increase that, and if we do it in revenue neutral fashion, that is something we would very much be interested in discussing.

Mr. ENGLISH. You would specifically say that you would be receptive to our looking at the section 179 expensing for small business?

Secretary RUBIN. Tell me what 179 is, and I will give you an answer. That is the expensing for small business?

Mr. ENGLISH. Yes.

Secretary RUBIN. That is right, I remember that. I had forgotten the number. I know the concept.

I think if you were to look at it and come to us with a proposal that was revenue neutral, then that is something we would be interested in discussing. The President originally wanted to have $25,000, and it turned out we have $17,500 or some such number, because that was the resolution we made with Congress.

Mr. ENGLISH. Thank you for your openmindedness. We appreciate your testimony today.

I would now like to recognize Mr. Cardin who will inquire.

Mr. CARDIN. Thank you, Mr. Chairman.

Secretary Rubin, thank you for your testimony. It has been a long morning for you between the Senate and the House, and we thank you very much for your patience and for your service to our country.

It is also refreshing to see that the predictions that were made in 1992–93 when you were working up the economic plan, following up on Mr. Payne's questioning, have really been consistent to what you present now 2 years later, and that the economic plan that you brought forward with the Clinton administration has in fact reduced the growth of our deficits, as was predicted.

I also remember very vividly listening to President Clinton's predictions that if we did not do health care reform, that much of the progress on deficit reduction would be lost, that Medicare and Medicaid and the entitlement programs were the fastest growing part of the budget, and we had to get health care reform under control if we were going to deal with the deficit and get it back to a balanced level.

I really do applaud you, because, yes, we could have irrational Medicare cuts in here, but, as I understand it, the administration is taking the position that it is not rational just to cut Medicare and shift the cost to private payors or to wreck the program that provides seniors with their health care, that that would not be a rational economic program to bring forward. So you have deferred, I assume, Medicare to when we get to health care reform, and I think that is obviously the right way to proceed.

If I might, let me get to what you have done on spending, on discretionary spending. How much growth do you allow during this period in discretionary spending?

Secretary RUBIN. Mr. Cardin, in this budget we project discretionary spending in each of 5 years after 1995 that is at a lower level than it was in 1994. So what you actually have is you have I think $555 billion in 1995, is my recollection of the number, and every year thereafter you have a lower number with respect to discretionary spending.

If I recollect correctly, in the last year of that 5-year period it is $549 billion. Not only is it lower, though, in nominal terms, but if you think of it in an inflation adjusted sense—after all, $100 today is worth a lot more than $100 5 years from now, because of inflation—so in an inflation adjusted sense, it is less by a lot more than it is in the pure nominal sense that I have just described.

Mr. CARDIN. So what you have brought forward is even larger cuts than what we call a hard freeze, no growth, no inflationary adjustment. That is the most aggressive attack on spending I think any administration has brought forward.

Secretary RUBIN. Mr. Cardin, I think we need to look, and we will look, to see what it looks like. My guess would be that it has been a long, long, long time since anybody has put forward a budget with realistic projections that project discretionary spending being lower in the 5 years of the budget than it was in the year preceding that.

I will tell you, to get there has taken a lot of tough, tough cuts, because we not only, as I said a moment ago, are having discretionary expenditures below the current year, but we lose because of the effects of inflation each year, and so that makes the cutting process even tougher.

Mr. CARDIN. I appreciate that, because it is very difficult to have a freeze. We have not been able to do that in too many years, actually hold the line on discretionary spending in this country, and I applaud you for bringing forward a budget that actually goes below a hard freeze, and on inflated dollars it is much more dramatic progress on reducing spending in this country. That has not been the case. We have not seen prior administrations bring anything like that forward.

It is interesting to point out that we have a lot of rhetoric from members of this committee about reducing the deficit, and yet I do not know of any proposals that have been made from the other side of the aisle at all on spending cuts to get us anywhere close to what your budget does in deficit reduction. We have a lot of specifics on tax cuts, but we do not have anything specific on spending cuts that will give us the type of deficit performance that you have brought forward.

I hope we can reduce the deficit more aggressively, but let us come forward with specific recommendations on spending cuts, rather than these generalities that it would be nice to reduce the deficit.

Thank you.

Mr. ENGLISH. Thank you.

Mr. McDermott will inquire.

Mr. MCDERMOTT. Thank you, Mr. Chairman.

I want to thank you for coming and for your testimony. As you notice now, all the Republicans have left, especially the ones who were badgering you about not being here early, so I guess they could not wait to hear the answers.

I just want to ask one parochial question. Bonneville Power Administration is not on the sale list of this budget, as I understand it. Is that correct?

Secretary RUBIN. That is correct, Mr. McDermott.

Mr. MCDERMOTT. You are talking about a public corporation, but not privatizing the Bonneville Power Administration.

Secretary RUBIN. We do not plan to sell the Bonneville Power Authority.

Mr. MCDERMOTT. I want to ask one other thing. Everybody talks about this balanced budget, and I know you know more than I do about money. You know way more than I do about money, but I have a feeling that what is being attempted here by these people who say they are going to balance the budget by the year 2002 is simply not good public policy. Certainly it is politically possible, but it is not good public policy.

The Joint Tax Committee yesterday, I think, came out with numbers of about $750 billion that would be needed to pay for the tax cuts. Do those figures square pretty much with what the Treasury has put out?

Secretary RUBIN. Yes, Mr. McDermott. We originally estimated that the Contract With America would result in something over 700 billion dollars' worth of costs or increase in deficit which would have to be made up through whatever programs determined it is to be made up with. We were somewhat criticized at the time for that number, but the Joint Tax Committee has now come up with a number of something in excess of $700 billion that these Contract

With America tax cuts will cost, so roughly speaking corresponds to our own numbers.

Mr. McDERMOTT. The members who are pushing this are blithely going along, as Mr. Cardin suggests, talking about what we will be able to do, that we will be able to do it.

My mother watches C-SPAN and she is 85 years old, and she does not really understand all of how the Federal budget is put together. It would be helpful I think for all of us to understand what really has to go into reaching 750 billion dollars' worth of cuts.

Secretary RUBIN. Let me go at it just a little bit differently, if I may, Mr. McDermott. I think the problem that we have with the balanced budget amendment and having an arbitrary date by which you must balance the budget, as opposed to really tough-minded fiscal discipline where you each year make a decision based on what seems to be in the best interest of the economy that year, puts you in a straightjacket, and then you have to do what the balanced budget amendment requires, regardless of economic circumstances. In our opinion, that is a dangerous position to be in.

Now, if you take the arbitrary date of 2002, we have estimated that if you take the tax cuts you have just mentioned, plus that which is requisite to meeting balance, it is going to cost you about $1.6 billion. I do not know quite how you get to that.

Mr. McDERMOTT. To $1.6 trillion?

Secretary RUBIN. Yes, $1.6 trillion. The $1.6 billion we could figure out—$1.6 trillion. I do not know how you get there other than to either decimate the discretionary side of the budget, that is to say education and training and Head Start and the programs that we think are critically important to the future of this country, or decimate defense or impose very substantial reductions on Medicare and Social Security. Those are your choices. There are no other choices, because that is the budget.

Mr. McDERMOTT. My mother lived through the depression. Let us say a depression occurred internationally in the next 5 years. What would that do to the straightjacket that you have then put the country into?

Secretary RUBIN. Well, my view—and I suspect this may correspond to your mother's, if she remembers the Keynesian economists of that last depression—my view is that what would happen is that we would be in a position where you have a depression that vastly increases the deficit and that deficit under ordinary circumstances would then be stimulative, and so it would bring you back out of the depression.

In fact, Mr. McDermott, with those automatic stabilizers—that is what they are called, in effect, you ought never really get into a depression, because as the economy slows down and the deficit starts to widen as a consequence, that deficit is stimulative and so that brings you back out of your slow growth or out of your recession.

Mr. McDERMOTT. That is what Franklin Delano Roosevelt was doing with the Public Works Administration and all the construction and all that sort of thing.

Secretary RUBIN. Precisely, that is exactly what happened during the——

Mr. McDERMOTT. So it actually increased the deficit during a recession?

Secretary RUBIN. Right, which is what you want to have happen, because the increased deficit will generate more economic activity and get you back out of the recession. The problem with the arbitrary date of 2002 is that if you go into a recession and you have that arbitrary date, you can't have those deficits, so, instead, you have to cut the deficit and that worsens the recession, that increases the deficit again, and then you have to cut that. What you really do is put yourself on a track toward either a horrendous recession or possibly something that could be called a depression.

Mr. McDERMOTT. Can you reassure us that there will be no events that will require from a fiscal policy the increase of the debt in the next 5 years?

Secretary RUBIN. I do not think, Mr. McDermott, anybody in the world could give you that assurance, and I think that is the problem with getting ourselves into arbitrary dates. It is why we so strongly advocate fiscal discipline accomplished through very careful, thoughtful, tough-minded decisions each year as to what we can accomplish in the context of the circumstances of that year.

I really do believe that an arbitrary date and a balanced budget amendment are dangerous public policies. I might add, as just an additional comment, that if one does feel that one wants to have a balanced budget amendment considered, then it seems to me what you should say to people is, if you are going to have a balanced budget amendment and balance by an arbitrary date, these are the cuts you are going to have to make, and then somebody could see whether the cuts that have to be made to get there by 2002 are worth getting to in an arbitrarily balanced budget by 2002. That is the way the debate should be framed, in our judgment.

Mr. McDERMOTT. Even with that, it would be risky, because you do not know what the factors will be between now and the year 2002.

Secretary RUBIN. Mr. McDermott, I think it is bad economic policy, period. But if you can get past that issue, which I would not get past, because I think it is bad policy, then it seems to me to say to people, to get there, we are going to have to do this to Social Security or that to Medicare or whatever the things are, defense or education or whatever, and then they can judge whether that tradeoff is worthwhile.

Mr. McDERMOTT. Thank you very much.

Mr. ENGLISH. Thank you very much, Dr. McDermott.

Thank you, Mr. Secretary, for your lengthy testimony today, as always, most eloquent. We appreciate your presence here.

Secretary RUBIN. Thank you, Mr. English.

Mr. ENGLISH. This committee stands adjourned until 10 a.m. tomorrow morning.

[Whereupon, at 1:27 p.m., the hearing was adjourned, to reconvene on Wednesday, February 8, 1995, at 10 a.m.]

PRESIDENT'S FISCAL YEAR 1996 BUDGET

WEDNESDAY, FEBRUARY 8, 1995

HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
Washington, D.C.

The committee met, pursuant to call, at 10 a.m., in room 1100, Longworth House Office Building, Hon. Bill Archer (chairman of the committee) presiding.

Chairman ARCHER. If our guests will take seats, please, we will commence. The Secretary is on a tight schedule, and we would like to proceed expeditiously.

Today we welcome the Honorable Donna Shalala, Secretary of HHS, Health and Human Services. Welcome back to the committee. You were here earlier this year. Without a doubt, this year is going to be a challenge for you, your department, and for us here on the Ways and Means Committee.

At the end of it all, I hope we will have turned that challenge into unquestionable success, for us and the government, the people that we serve. In the near future, the committee will begin markup of the welfare proposals that are part of our Contract With America, and this is going to be a sweeping change in the way our country provides assistance to low-income populations.

It will change not only the policy but the operation of your agency over at HHS. All of us want to make sure that it is good social policy and a system that your department can administer.

I can assure you that we are going to be working with you to reach that outcome. The Speaker has asked me and my colleague, Mr. Thomas, to look into transforming Medicare, taking a creative approach not solely to reduce costs but to design a program for the 21st century, not the sixties. We are going to need your help and that of your excellent technical staff in that endeavor.

Thank you again for joining us today. I am pleased to recognize Pete Stark for the opening statement of the minority.

Mr. STARK. Thank you, Mr. Chairman.

I am pleased to welcome Secretary Shalala for a discussion of the President's budget for fiscal year 1996. The President has chosen to keep reductions, happily, in Medicare to a minimum. The result is keeping Medicare savings to $140 million in 1996, and $9.8 billion over the next 5 years, a record that we in a bipartisan sense in the past have been able to achieve without disrupting the system through the cooperation of the then-minority, and the Republican and Democrat administrations over that period of time.

The President's approach is the correct approach. For 30 years, we have been working successfully to uphold the true contract with Americans, and that is Medicare. We have not and will not agree to breaking that contract in order to finance a Republican tax cut for the wealthiest people in this country.

The President has endorsed this approach in his budget, and we intend to follow his lead in protecting Medicare from mindless budget cutting. That is not to say we shouldn't work to reduce the growth rate in Medicare.

This committee proposed last year in its health reform bill several cuts, and we maintained the solvency of Medicare. It is required that we do so. But mindless slashing of Medicare will only disrupt the health services on which America's seniors depend and will have a ripple effect into the entire health delivery system of this country.

It is the vulnerable parts of the health system, inner city and rural hospitals, teaching hospitals, centers of excellence, children's hospitals, all stand on the brink of destruction if we were to follow the Republican budget proposal and not the President's cautious and conservative proposal.

It makes sense to reform the health care financing system comprehensively, shoring up financing where it is needed and reducing financing where we can. That is the sensible way. It is more sensible than the Republican social policy, which is to give everything you can to the rich and find a way to pay for it by impacting the poor.

I know the Secretary joins me in resisting that policy, and we will work with you, Madam Secretary, to protect the most vulnerable people in this country, as your department has done for so many years. Welcome to the committee.

Thank you, Mr. Chairman.

[The prepared statements follow:]

Statement of the Honorable Pete Stark

February 8, 1995

Mr. Chairman, I am pleased to join in welcoming the Secretary of Health and Human Services for a discussion of the President's budget for fiscal year 1995.

I am very pleased that the President has chosen to keep reductions in Medicare to a minimum. The result is to keep Medicare savings to $140 million in FY 1996 and to $9.8 billion over the next five fiscal years.

The President's approach is the right one. For 30 years we have been working successfully to uphold the true contract with America -- Medicare. We have not and will not agree to breaking that contract in order to finance today's Republican tax cuts for the wealthiest. The President has endorsed this approach in his budget, and I intend to follow his lead in protecting Medicare from mindless budget cutting.

That is not to say that we should not work to reduce the growth rate in Medicare, as this Committee proposed last year in its reported health reform bill. Maintaining the solvency of Medicare requires that we do so. However, mindless slashing of Medicare will only disrupt the health services on which America's seniors depend. It is the vulnerable parts of the health system, such as inner city and rural hospitals, which bear the brunt of that approach.

It makes far more sense to reform the health care financing system comprehensively, shoring up financing where needed, and reducing financing where we can. That is the sensible way to reach the goals we share. I want to work with you Madame Secretary to do just that.

Thank you, Mr. Chairman.

Jim Ramstad

STATEMENT OF REPRESENTATIVE JIM RAMSTAD
WAYS AND MEANS COMMITTEE
HEARING ON CONTRACT WITH AMERICA
February 8, 1995

Mr. Chairman, I appreciate the opportunity to speak with Secretary Shalala about the health care provisions in President Clinton's 1996 Budget.

As I mentioned to Secretary Rubin yesterday, I am disappointed in the President's newly-released budget.

President Clinton missed an excellent opportunity to work with Congress on significant deficit reduction. As the President explained last year, we will never reduce the massive budget deficit without stemming the astronomical rise in federal expenditures on health care.

I believe we must fundamentally restructure the system currently in place to finance these public health programs. The private sector has gone through dramatic changes in recent years, resulting in significant control of the rise in health care costs. It is essential to bring similar changes to public health programs.

Mr. Chairman, thanks again for calling this hearing. I look forward to hearing Secretary Shalala's testimony and to exploring in greater depth this important issue.

Chairman ARCHER. Madam Secretary, we would be pleased to receive your oral testimony. If you have a lengthier written testimony, all of it without objection will be inserted in the record.

You may proceed.

STATEMENT OF HON. DONNA E. SHALALA, SECRETARY, U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES

Secretary SHALALA. Thank you very much, Mr. Chairman, and members of the committee. Thank you for giving me the opportunity to appear before you to discuss the President's 1996 budget.

We believe this budget is another bold step toward fulfilling the President's commitment to put people first, and to address the long-term challenges facing this country. The Health and Human Services budget request is $716 billion, a 7.5-percent increase over the 1995 budget.

The increases in the entitlement budget represent 98 percent of our overall budget growth. Our budget for discretionary programs is $37 billion, an increase of $1.5 billion or 4 percent over last year.

This budget reflects the core values of the Clinton administration. We believe government must focus on the everyday needs of American people. We believe government should empower people to take greater responsibilities over their own lives. We believe that local communities know what their problems are and that they should be the driving force in fixing them.

We believe that certain jobs now done by the Federal Government should be turned back to the States. But we also believe that some issues require leadership at the Federal level.

We believe that there is an important role for the Federal Government in protecting the elderly, the disabled, and children, in conducting basic scientific research and ensuring that all of our children receive immunizations and a head start in life.

We are fundamentally changing the way the government works to serve the American people better. In our 1996 budget, we look seriously at our discretionary programs to find opportunities to cut spending, to seriously consolidate services, and to do more with less.

In fact, we reduce categorical programs in this budget by 22 percent departmental wide. We consolidate 108 PHS activities into 16 performance partnerships to give States greater control, greater flexibility, and greater accountability.

We reduce funding for 69 programs, taking them below the levels approved by Congress in the 1995 budget. We froze an additional 57 program activities at their 1995 levels.

These savings are real. But they don't represent the full scope of our achievement in reducing the deficit. The most dramatic success story in this budget is our ongoing effort to reduce the rate of growth in health-related entitlement programs.

We are now finding that for the period 1994–98, spending on entitlements is likely to be a whole lot less than it was projected to be when the President took office in 1993. To be precise, $212 billion less. I mean billion with a "B."

For the first time since 1988, the anticipated growth in Medicare and Medicaid dropped below double digits, from 12.7 percent a year to 9.5 percent—the chart here shows that drop—reducing our expected deficit and the debt burden we leave to future generations.

I would like to take 1 minute to talk about several factors contributing to reduction in the projected growth of Medicare and Medicaid. In 1993, this administration worked successfully with the Congress to enact the largest deficit reduction bill in history.

This tough spending program was designed to reduce projected deficits by $500 billion over 5 years. Because the economy has responded so strongly, experts now predict our deficit will drop by more than $600 billion.

The President's economic program has curbed both the general and health care inflation. That has built a framework for our improved picture on entitlement spending, and we have been working hard to make sure that that picture doesn't change.

We appreciate and noted the bipartisan support Congress gave to the 1991 legislation on taxes and donations, which limits inappropriate Medicaid financing schemes used by the States. Today we are working in partnership with the States to narrow those loopholes. That saves us money.

We are aggressively managing our Medicare and Medicaid programs, replacing five underperforming Medicare contractors over the past 2 years, and we are waging an all-out attack on waste, fraud, and abuse.

In 1994 our Inspector General helped recover and save $5.4 billion in Medicare and Medicaid. Across the Department, we have recovered and saved more than $8 billion.

That is the largest amount ever in the history of the Department in 1 year. In addition, last year coordinated efforts among our Inspector General and several other Federal and State agencies yielded the largest single health care fraud settlement in history, totaling a record of $379 million. These are major accomplishments. But the American people deserve more.

We will intensify our assault on waste, fraud, and abuse. To accomplish this we are considering as part of Reinventing Government II a new innovative program with stable and reliable funding. We will focus our efforts on parts of the country where the problem is the greatest, on those activities that achieve the most effective results.

We are also changing the way Medicare and Medicaid work to improve quality, to promote efficiency, to lower costs, and give the American people more health care choices.

More and more States are taking advantage of new opportunities to offer managed care programs under Medicaid. More and more health plans and individuals are choosing the managed care option under Medicare.

Last year, Medicaid had a 63-percent increase in the number of Americans enrolled in managed care plans, from 4.8 million people in 1993 to 7.8 million in 1994. In addition, the number of older Americans choosing managed care through the Medicare program grew by 16 percent, from about 2.7 million people in 1993 to more than 3.1 million in 1994.

We expect it to grow by another 20 to 25 percent next year.

Managed care's emphasis on prevention and primary care is cost effective, and particularly for Medicaid customers, much less expensive than reliance on emergency health services.

We note that American people appreciate being able to choose managed care options, and we are committed to preserving and enhancing those choices. Our commitment to expanding health care options extends beyond the Medicare and Medicaid programs, and that is why the President has asked both Democrats and Republicans in Congress to work with him to expand insurance coverage for the American people, and to contain health costs for families, businesses, and governments.

There are many other exciting things to say about health care, but for now, I would like to turn to another equally important service, Social Security. We have got a great story to tell here, too. Our Social Security Administration has completely overhauled the way it does business, providing better and faster service.

By the end of 1996, people will no longer have to wait 100 days or more for disability claims to be processed. We will have cut the time by one-third. At any time, no matter how old you are, you can write to find out how much you have contributed to Social Security, and obtain an estimate of your potential monthly benefits when you retire.

We will tell you promptly, in words that make sense. I know, because I did it myself.

The SSI program has received a lot of attention lately, and we are working to reshape this program to better serve both taxpayers and those it was intended to help: disabled children and their families. Among other things, we have appointed a Childhood Disability Commission headed by former representative Jim Slattery.

Just a few weeks ago, I had the privilege of appearing before this committee to discuss another issue, welfare reform. Since that time, we have all been encouraged by the bipartisan commitment to overhaul our broken welfare system, as evidenced by the President's recent working session on welfare reform and the ongoing work of this committee.

As the committee prepares to mark up its legislation, this administration looks forward to working with you to move Americans from welfare to work.

Mr. Chairman, I believe that we are standing at an important crossroads in American history. The American people are frustrated with government, and they want real change. They have challenged us to join hands to make government work better, to make it cost less, and to reflect the core values of our country. Over the last 2 years, that is just what we have done.

Throughout our department we have enhanced customer service and achieved real results. For example, immunization rates for preschool children are now at their highest in American history. We have granted more health care and welfare waivers than any other administration. Head Start is improving its quality and serving more children than ever before.

At the National Institutes of Health, we have made critical breakthroughs in basic medical and science research, in areas ranging from AIDS to breast cancer, from sickle cell anemia to the Human Genome project. We look forward to working with you to achieve even more.

I greatly appreciate the opportunity to testify before you this morning and I would be happy to answer any questions.

[The prepared statement follows:]

STATEMENT OF DONNA E. SHALALA, SECRETARY
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES

Good morning. Mr. Chairman and members of the Committee. Thank you for giving me the opportunity to appear before you today to discuss President Clinton's 1996 Budget.

This budget is another bold step towards fulfilling the President's commitment to put people first and address the long term challenges facing this country.

The HHS budget request is 716 billion dollars, a 7.5 percent increase over the 1995 budget.

Increases in the entitlement budget represent 98 percent of our overall budget growth.

Our budget for discretionary programs is 37 billion dollars, an increase of 1.5 billion dollars or 4 percent, over last year.

This budget reflects the core values of the Clinton Administration:

We believe that government must focus on the everyday needs of the American people.

We believe that government should empower people to take greater responsibility for their own lives.

We believe that local communities know what their problems are -- and they should be the driving force in fixing them.

We believe that certain jobs now done by the federal government should be turned back to the states ...

... but we also believe that some issues require leadership at the federal level.

We believe that there is an important role for the federal government in protecting the elderly and disabled, conducting basic scientific research, and ensuring that our children receive immunizations and a Head Start in life.

We are fundamentally changing the way that government works to serve the American people better.

In our 1996 budget, we looked seriously at our discretionary programs to find opportunities to cut spending, consolidate services, and do more with less.

In fact, we reduced categorical programs by 22 percent department-wide.

We consolidated 108 PHS activities into 16 Performance Partnerships to give States greater control, flexibility, and accountability.

We reduced funding for 69 programs, taking them below the levels approved by Congress in the 1995 budget.

We froze an additional 57 program activities at their 1995 levels.

These savings are real -- but they don't represent the full scope of our achievements in reducing the deficit.

The most dramatic success story in this budget is our on-going effort to reduce the rate of growth in health-related entitlement programs.

We are now finding that, for the period from 1994 to 1998, spending on entitlements is likely to be a whole lot less than it was projected to be when President Clinton took office in 1993.

212 billion dollars less, to be precise.

Yes, that's "billion" with a "b."

For the first time since 1988, the anticipated growth in Medicare and Medicaid dropped below double digits -- from 12.7 percent a year to 9.5 percent, for the period from 1994 to 1998.

Since the 1993 projections, anticipated growth in Medicare has dropped from an average of 11.9 percent per year to an average of 9.9 percent per year from FY 1994 to FY 1998.

That reduces projected expenditures by 79 billion dollars over five years.

Expected growth in Medicaid has fallen from 13.9 percent per year to 8.7 percent from FY 1994 to FY 1998. That results in projected spending that is 133 billion dollars lower over the same five-year period.

And this difference goes straight to the bottom line, reducing our expected deficit and the debt burden we leave to future generations.

I'd like to take a minute to talk about several factors contributing to the reduction in the projected growth of Medicare and Medicaid.

In 1993, this Administration worked successfully with the Congress to enact the largest deficit reduction bill in history.

This tough spending program was designed to reduce projected deficits by 500 billion dollars over five years.

And, because the economy has responded so strongly, experts now predict that our deficit will drop by more than 600 billion dollars.

The President's economic program has curbed both general and health care inflation.

That's built the frame for our improved picture on entitlement spending.

And we've been working hard to make sure that picture doesn't change.

We appreciate the bipartisan support Congress gave to the 1991 legislation on taxes and donations, which limits inappropriate financing schemes used by states.

Today, we're working in partnership with the states to narrow those loopholes -- and that saves us money.

Our aggressive management of the Medicare and Medicaid programs is also keeping spending in check and improving program efficiency.

Over the past two years, we've replaced five underperforming Medicare contractors.

And our oversight of the other Medicare contractors has resulted in more efficient provider payments.

We're also waging an all-out attack on waste, fraud and abuse.

In 1994, our Inspector General achieved more than 1,500 successful prosecutions and administrative sanctions in Medicare and Medicaid -- which, combined with legislative and regulatory changes -- helped secure 5.4 billion dollars in savings for the American people.

And, across the Department, we recovered and saved more than 8 billion dollars -- that's the largest amount ever by HHS in one year!

In addition, last year, coordinated efforts among our Inspector General and several other federal and state agencies yielded the largest single health care fraud settlement in history.

A firm with more than 60 psychiatric hospitals agreed to pay back the Federal government a record 379 million dollars.

These are major accomplishments -- but the American people still deserve more.

We will intensify our assault on waste, fraud and abuse. To accomplish this, we are considering as part of Reinventing Government II, a new innovative program with stable and reliable funding.

We are also going to focus our efforts in parts of the country where the problem is greatest -- and on those activities that achieve the most effective results.

But that's not the only part of the Medicare and Medicaid programs that we are reinventing.

We have approved more health care waivers than any other Administration, providing states the flexibility to address their own health care issues with their own solutions.

We're also changing the way Medicare and Medicaid work, to improve quality, promote efficiency, lower costs, and give the American people more health care choices.

More and more states are taking advantage of new opportunities to offer managed care programs under Medicaid.

And, more and more health plans and individuals are choosing the managed care option under Medicare.

Last year, Medicaid had a 63 percent increase in the number of Americans enrolled in managed care plans -- from 4.8 million people in 1993 to 7.8 million in 1994.

In addition, the number of older Americans choosing managed care through the Medicare program grew by 16 percent -- from about 2.7 million people in 1993 to more than 3.1 million in 1994.

And we expect it to grow another 20 to 25 percent next year.

Managed care's emphasis on prevention and primary care is cost-effective, and, particularly for Medicaid customers, much less expensive than a reliance on emergency health services.

We know the American people appreciate being able to choose managed care options -- and we are committed to preserving and enhancing those choices.

Of course, our commitment to expanding health care options extends beyond the Medicare and Medicaid programs.

That's why the President has asked both Democrats and Republicans in Congress to work with him to expand insurance coverage for the American people, and to contain health costs for families, businesses and governments.

There are many other exciting things to say about health care. But for now, I'd like to turn to another, equally important service: Social Security.

And we've got a great story to tell here, too.

The Social Security Administration is completely overhauling the way it does business -- providing better and faster service.

By the end of 1996, you will no longer have to wait 100 days or more for your disability claim to be processed -- we will have cut that time by a third.

At any time, no matter how old you are, you can write to find out how much you have contributed to Social Security and obtain an estimate of your potential monthly benefits.

We'll tell you, promptly, in words that make sense.

I know -- because I did it myself.

The SSI program has received a lot of attention lately -- with allegations about parents using their children as pawns to rip off the system and cheat the taxpayers.

In May of 1994, our Inspector General completed a study of about 600 cases of children receiving SSI because of behavioral or learning problems.

The Inspector General found no evidence of widespread coaching by parents.

But, even one case is too many -- and that's why we are taking strong steps to stop these abuses once and for all.

Among other things, we've appointed a Childhood Disability Commission, headed by former Representative Jim Slattery.

I have asked them to complete their report as quickly as possible and recommend ways that we can reshape the program to better serve both taxpayers and those it was intended to help: disabled children and their families.

In addition, the Administration is conducting its own review of all our disability policies to assure strong, efficient protection of people with disabilities.

* * *

Just a few weeks ago, I had the privilege of appearing before this committee to discuss welfare reform.

Since that time, I have been encouraged by the bipartisan commitment to overhaul our broken welfare system -- as evidenced by the President's recent working session on welfare reform and the on-going work of this Committee.

As the committee prepares to mark up its legislation, this Administration looks forward to working with you to move Americans from welfare to work.

Mr. Chairman, I believe we are standing at an important crossroads in American history.

The American people are frustrated with government -- and they want real change.

They've challenged us to join hands to make government work better, cost less, and reflect the core values of our country.

And, over the last two years, that's just what we've done.

We've made accountability the watchword of this department by consolidating programs, slashing administrative costs, and cracking down on waste, fraud, and abuse.

We've granted more health care and welfare waivers than any other Administration -- thereby giving states and local communities the flexibility to solve their own problems.

We've enhanced customer service in countless ways:

For example, we have improved our home and community-based long term care programs ...

... and we have brought Medicare and Medicaid into the 21st century with cost-saving, state-of-the-art technology that will empower people to make more informed choices about their health care.

Throughout our department, we've demanded quality and achieved real results:

Immunization rates are at their highest in history.

Head Start is improving its quality and serving more children than ever before.

And, at the NIH, we have made critical breakthroughs in basic medical and scientific research in areas ranging from AIDS to Breast Cancer and from Sickle Cell Anemia to the Human Genome Project.

We're proud of these accomplishments -- and, we look forward to working with all of you to achieve even more.

I greatly appreciate the opportunity to testify before you this morning. I'd be happy to answer any questions. Thank you.

Chairman ARCHER. Thank you, Madam Secretary. I am going to yield my time for questioning to Mr. Crane.

Mr. CRANE. Thank you, Madam Secretary.

How does the projected rate of growth for Medicare and Medicaid compare with the cost of coverage in the private sector?

Secretary SHALALA. It is ahead of the private sector, and there is no question about that. The only point that I was making here was that it is starting to come down, and that is because of legislation that was passed, the impact of bringing down the deficit, the slowdown in inflation, the private sector beginning to slow down, particularly the large corporations who are negotiating tough deals with hospitals. So there are lots of things going on.

But we still are very much above private sector growth and health care costs. We deal with different populations, Congressman Crane.

Mr. CRANE. Is it the different populations you are dealing with that create that disparity in costs in the private sector versus Medicare and Medicaid?

Secretary SHALALA. The difference between the growth in the government programs and growth in the private sector is the result of a combination of factors. From 1984 to 1993, for instance, the Medicare growth per enrollee was less than the private sector. Starting in 1994, we are ahead of the private sector. But the slowing down of growth rates that I reported today means that we are getting on top of some of the things that were happening, including the creative use of provider taxes and other kinds of things by the States which the Congress closed down.

It would be too early to say that we are going to get down to where the private sector is because of the difference in population. Remember, the health care programs in the government deal with long-term care for a highly vulnerable population. We are the major providers of health care to the disabled, to the severely disabled. We have the elderly population.

So one should expect some changes, but we also can demand real discipline in the management in the programs, in our anticipation of how the programs work. I think the efforts that have been made are reflected in the baseline starting to come down.

Mr. CRANE. I know there is an effort being made in the private sector to streamline, figure out how to economize. I was wondering if there are any other changes in Medicare to attempt to replicate some of that streamlining and cost cutting in the private sector that are being contemplated.

Secretary SHALALA. Yes, sir. Our consolidation of our computer systems, the better management of the private insurance companies that are managing the Medicare program, doing real analysis on what is happening to home care costs, there are lots of things going on within the Medicare program.

The movement of people in both Medicare and Medicaid to managed care, while in Medicaid it may produce some savings, in Medicare it has not yet produced the kinds of savings we would like to see. We have a lot more to learn about managing that program. So there is a lot of work to be done.

But the kinds of things the private sector is doing are helping public sector programs at the same time. It is, however, not helping the smaller markets, the small business people who don't have the kind of clout that the large corporation does coming in to negotiate. So the context still has to be comprehensive health care reform.

We can do only so much to reduce costs through managing these programs. Comprehensive health care reform, reducing the number of people who are walking into emergency rooms, that are not getting preventive care, dealing with long-term care issues—there are a lot of things in cost containment that have to be part of a comprehensive effort, and that is why the President still believes that in a bipartisan way, we ought to sit down and work on comprehensive health care reform.

Mr. CRANE. Does HCFA provide unlimited latitude to States in dealing with the Medicaid question, to in effect put those folks into managed care or health maintenance organizations?

Secretary SHALALA. We have worked closely with a number of States who wish to move their beneficiaries into managed care. I think if you spoke to the Governors across the country, they would say there has been a new atmosphere in terms of our relationship.

I recently talked to a Governor who wanted to move many of his beneficiaries into managed care, and he said that the questions he got back from HCFA which made him reshape his strategy but stick with his goal were extremely helpful. His staff hadn't thought of them, and he liked the going back and forth of working through the waivers. So I think we have a healthy relationship with the Governors, and they know that we very much want to work with them on these issues.

Mr. CRANE. One final question. Medicare part B is a very expensive welfare program. Initially at its outset my understanding is 50 percent was paid by the individuals, and that that is down to about 31 percent today.

In your estimation, should that be raised back to the 50-percent figure?

Secretary SHALALA. We have favored the deal that was cut with the beneficiaries at around 25 percent, which we think is fair. But again, any review of the payment mix ought to be part of a comprehensive effort to review health care programs, because what we are all trying to do is to hold down the cost of health care in the public sector without shifting it onto the private sector, to be fair to beneficiaries.

The mix of what beneficiaries pay is very much a fairness issue. Our only plea is that we do all of this within the context of overall health care reform so we don't have the health care costs popping up in the private sector because we have shifted them to the private sector.

Mr. CRANE. Thank you, Madam Secretary.

Secretary SHALALA. You are welcome.

Chairman ARCHER. Mr. Stark.

Mr. STARK. Thank you, Mr. Chairman.

Madam Secretary, I must say I was more than pleasantly surprised by the size of the Medicare cuts that the President put forth in his budget. I don't want to help my Republican colleagues out of their dilemma of how they can possibly pay for this silly contract. But I had anticipated somewhat larger cuts, not the $200 billion they are talking about, but yours seem rather modest.

In light of this idea that Medicare is going to go broke one of these days, why are your cuts at the level they are, and can you give us a reassurance that 10 years from now we will still be around discussing Medicare?

Secretary SHALALA. I think there are two questions there, Congressman Stark. One is our concern about the financing of the Medicare program. I am a trustee of the system along with Secretary Reich and now Secretary Rubin. In terms of any thoughts we have on the financing of the system, the trustees will meet again in April and have some new actuarial estimates and then we will come back and talk with all of you about that information.

On the issue of the President simply extending existing restraints on the Medicare program as opposed to adding new ones, he has always said that he is willing to consider changes in the government's health care programs, in particular the Medicare program, but only in the context of health care reform.

Both in his letter to the Congress, as well as in his State of the Union speech, as well as in the language in this budget where health care reform is discussed, he has made it very clear he opposes cutting Medicare to finance tax cuts. He opposes cutting Medicare just to reduce the deficit, outside of the context of health care reform.

So we are anxious to start the discussion with this Congress on taking some steps toward health care reform, and would be happy to discuss these programs within that context.

Mr. STARK. The Republicans are suggesting, I guess in the words of Speaker Gingrich, that we eliminate the Health Care Financing Administration. I notice that Mr. Vladeck is not here today. I assume that doesn't indicate it has already been done.

Can you explain to me and my colleagues and for the record why the Health Care Financing Administration is a necessary operation in the Department of Health and Human Services, and why Mr. Gingrich should perhaps rethink his rash suggestion?

Secretary SHALALA. Thank you, Congressman.

The Health Care Financing Administration and the management of the government's health care programs are best seen in the context of a public-private partnership. In fact, unlike Social Security, which is totally managed by public sector employees, the Medicare and Medicaid programs are managed—and the Medicare program particularly—is managed by the private sector. What HCFA does is manage the contractors, the private sector insurance companies, and does oversight over the private and nonprofit facilities that deliver health care in this country.

HCFA actually is quite efficient. It manages the government's program with an overhead of less than 2 percent. I don't know of an insurance company that would be willing to take on these programs for 2 percent or less in terms of its management.

There aren't a lot of employees there. What they are doing is managing this public-private partnership. The government sets the rules for the programs. But the management is very much private sector management, large contractors.

So it is not—we have moved away from government just running the program directly as we have in the Social Security program to this public-private partnership in which 99 percent of the employees that are involved in the government's health care program are private sector doctors, physicians, insurance companies who are managers of the system.

Mr. STARK. Don't we return about 97 or 98 cents of every $1 we collect to the system for health care benefits for the seniors under Medicare?

Secretary SHALALA. Yes, and that is the point I am making, that the money goes out to the delivery system, to the private sector, to health care, as opposed to having a huge bureaucracy in Washington. It actually is a very thin layer, managing what are essentially private sector contracts. That was the decision early on in terms of the evolution of the program.

I also think that we get a lot of bang for the buck from HCFA. They really see themselves as partners with the States in the Medicaid program working through, for instance, this new and I think quite exciting movement to manage care, working with the States, using the experience around the country, working within individual States to help them set up the capacity to move beneficiaries into managed care, and making certain there is choice for elderly citizens, managed care, other kinds of options for them.

Chairman ARCHER. The time of the gentleman has expired.

Mr. Thomas.

Mr. THOMAS. Thank you very much, Mr. Chairman.

Yesterday, Secretary of the Treasury, Mr. Rubin, in his presentation indicated that if we were ever going to get a handle on the deficit, that the entitlements were the area that we were going to have to begin to control. He referred specifically to Medicare as one of the larger ones, and obviously Social Security is as well.

Last year the President offered a very ambitious, flawed but bold, plan to deal with this very question. As I recall, he had $124 billion in cuts in Medicare over 5 years.

You have shown us a chart in which the January 1993 projected baseline has been cut by that yellow amount to the Clinton 1996 baseline. It says, Medicare and Medicaid growth slows under the Clinton administration.

Would you agree that the single biggest impact was the $56 billion in Medicare cuts that were included in the budget reconciliation in 1993?

Secretary SHALALA. No, actually, as I indicated, this is a $200 billion reduction in the baseline over time. There were lots of explanations for——

Mr. THOMAS. Would you agree that one of them was $56 billion in Medicare cuts in the 1993 budget?

Secretary SHALALA. Certainly. We did those as a buildup to health reform.

Mr. THOMAS. Then you offered $124 billion in Medicare cuts after the $56 billion in Medicare cuts. Then in this budget, the last budget that President Clinton knows he has complete control over, what are the Medicare cuts? What was the amount that Mr. Stark raised?

Secretary SHALALA. The baseline would be reduced about $13 billion.

Mr. THOMAS. About $13 billion, 9.9 is the actual budget figure. When Secretary Rubin says it is critical to address this area, the

Clinton budget response, the last budget he has complete control over, there is a $9.9 billion response.

I guess in today's Post it says it best, and I hate bringing in a third-party neutral objective position. I know how folks don't like to do that. Jim Glassman in today's business section, headline on deficit cutting, Clinton Simply Gives Up the Ship. Balancing is up to the GOP.

I don't think it can be underscored more than by looking at what the Clinton administration promised it was going to do during the election, cut the deficit in half, by the bold $56 billion move which is reflected in this chart, following up with the bold $124 billion move in the health care reform, and then taking a look at the $9.9 billion response. You have given up the ship in the direction of balancing the budget.

I guess my question, Madam Secretary, is what was left on the budget cutting room floor behind closed doors that would have assisted us working as a partnership to solve this problem that you folks clearly understand to be a problem?

Secretary SHALALA. A spirit of bipartisanship, a desire to steer that ship in a bipartisan manner within the context of health care reform. The decision that was made was not to back off from this country's need to do health care reform and comprehensive health care reform as a way to continue to pull down that baseline and that growth.

So our commitment was not to back off of health care reform, but to do it in a bipartisan manner and to be ready within the hour to sit down with you and your colleagues to look at drafting a bill for comprehensive health care reform that will in fact not cause a cost shift to the private sector, in particular to small businesses in this country.

Mr. THOMAS. In that regard, is the administration going to support us in the effort to make permanent Medicare Select which is currently the only real ability to get managed care effectively into the Medicare structure?

Secretary SHALALA. The administration has always been committed to the issue of choice, and would be happy to work with this committee to expand choice for Medicare recipients. We have some concerns growing out of the Medicare Select demonstrations that have been going on, and we would like to discuss those with you within the context of a discussion about choice and about expanding choice.

Mr. THOMAS. Once again, the headline. On deficit cutting, "Clinton Simply Gives Up the Ship. Balancing is Up to the GOP." We are willing to do the heavy lifting if you are willing to help us.

Thank you, Mr. Chairman.

Chairman ARCHER. Mr. Bunning.

Mr. BUNNING. Thank you, Mr. Chairman.

I would like to shift gears here just a little bit, Madam Secretary, because of my interest in the Social Security Administration. Social Security benefits and SSA operating administrative budgets are independently funded from the trust funds, which you know will have reserves of about $420 billion this year. SSA administrative budget requests for 1996 are just a little over $6 billion, less than 2 percent of what SSA pays out in benefits.

Would you agree that the reserves appear to be more than adequate to absorb a $6 billion administrative budget?

Secretary SHALALA. You are asking me a policy question that I am not sure I am prepared to answer here. I think I'd better provide the answer to that question for the record, Mr. Bunning.

[The following was subsequently received:]

As you know, Congress has authorized a mix of funding for SSA's principle administrative account—the LAE, limitation on administrative expenses, account. The LAE account provides resources for SSA to administer the Social Security (OASDI) programs, certain health insurance functions, and the SSI program for the aged, blind, and disabled. Funds for annual reporting of earnings and certain activities related to pension reform also are included, as well as automated data processing and telecommunications expenses.

Currently, administrative expenses are financed from several different sources. In fiscal year 1994, for example, nearly 48 percent of the LAE account was financed by the Medicare trust funds and SSI program, while about 52 percent was financed by the OASDI trust funds. Congress has authorized this mix of funding because the Social Security trust funds and SSI service delivery mechanisms are so integrated—and we continue to support that approach.

Mr. BUNNING. The answer to that is obviously a yes. I mean, less than 2 percent or around 2 percent. Particularly since—by the end of fiscal year 1996, the Social Security trust funds will be about $540 billion in surplus.

For the record, since SSA is still part of HHS until March of this year, removing the SSA administrative budget from the domestic discretionary caps, would you be in favor of doing that?

Secretary SHALALA. I think that we thus far have not agreed to do that, and therefore we left the administrative budget for SSA under the discretionary caps. But you are raising an issue that we have discussed before within the administration. I would rather provide you with the official answer on that question.

[The following was subsequently received:]

We believe that keeping SSA's administrative expenses in the discretionary spending category provides a healthy tension that results in incentives for efficiency and encourages SSA to continue to provide service in the most productive, cost-effective manner.

Mr. BUNNING. Under the current rules, the SSA administrative budget is subject to the domestic discretionary caps, as we told you, even though SSA is independently funded by payroll taxes. Is that true or false?

Secretary SHALALA. It is funded by payroll taxes.

Mr. BUNNING. Does this mean even though it is independently funded, SSA has to fight against initiatives dreamed up by the administration for the resources it needs just to process its retirement and disability claims?

Secretary SHALALA. Well, if your general point is, are we prepared to move the administrative costs of the SSA budget under the entitlement side of the budget, I think our point is that we have not been willing to do that up until now. The administrative budget has always been on the discretionary side, Mr. Bunning.

Mr. BUNNING. Secretary Shalala, you realize there are over 1 million people backlogged in SSDI right now.

Secretary SHALALA. I do. Let me also point out that we have made an extraordinary effort to catch up on those and——

Mr. BUNNING. But we haven't. That simply is untrue. The fact of the matter is they keep growing. We keep spending more money to process it and the amount of disability claims keeps growing.

Secretary SHALALA. We have—our projections show that we will cut—with our reengineering proposals, that we will cut by one-third the amount of time it takes to get into the disability program.

Mr. BUNNING. I am not going to fight with you on that because I have no senior reengineering program. The Commissioner has not brought it forth for us to examine it yet. So how in the world can you say that you are going to cut by one-third when there is no positive proof that that is the case?

Secretary SHALALA. Those are our plans, Congressman Bunning.

Mr. BUNNING. I know. We spent $200 million extra to reduce the backlog 2 years ago. It was spent on bonuses for members of the Social Security Administration; 67 percent of the Social Security employees received bonuses. It didn't reduce the backlog.

So what I am saying is that we ought to at least take the administrative cost and put it on budget. Is the independent agency going to be able to do that? That is the question I am asking you.

Secretary SHALALA. The independent agency will not have the independent authority to move its budget from the discretionary side to the entitlement side without a congressional decision and a recommendation from the President.

Mr. BUNNING. It will not have the ability?

Secretary SHALALA. As far as I know, it does not have the authority under the Independent Agency Act.

Mr. BUNNING. It is my opinion that it will.

Secretary SHALALA. We will be happy to discuss that with you.

Mr. BUNNING. All right. Thank you.

Chairman ARCHER. Mr. Matsui.

Mr. MATSUI. Thank you, Mr. Chairman.

Secretary Shalala, thank you for your testimony today, we appreciate it very much. The one question that I have is, some have been talking about making massive cuts in the Medicare program without health care reform. The President's proposal last year in which he suggested cuts in Medicare was based upon health care reform, bringing everybody into the system and creating the system in which perhaps cuts could have been made because, obviously, there would have been a balancing.

But in terms of making cuts without health care reform, keeping the status quo, essentially, the fear that I think you and others have had is the issue of the cost shift. Would you get into that and talk about the cost shift and what would happen if in fact we made cuts that are being proposed in the Medicare system without health care reform.

Secretary SHALALA. Well, we testified last year at some length, Congressman, about our concern in doing health care reform in a way that simply drove down the cost of the government programs and then shifted those costs onto the private sector. We have even more concern this year about part of the private sector being able to pull down their own costs through tough negotiations with hospitals, with HMOs, and with other providers, which means that if we independently cut the Medicare program, for example, the group that we will be shifting costs onto will be even narrower. It will be small businesses, those that don't have the clout to get the kind of discounts that larger companies get.

So it becomes an even more serious problem when we narrow down the group to whom the costs will be cost shifted. We may well increase—as you well know, over 1 million people lost their health insurance last year. Most of them were working people, 85 percent. They don't even have access to adequate health insurance. So we are accentuating the problem by putting off comprehensive health care reform.

Mr. MATSUI. So you are saying that if in fact these cuts should occur, the shift, the cost shift will occur basically on small businesses, because they don't have the wherewithal to negotiate with insurance carriers, and undoubtedly those that would be affected by this would be employees of the small businesses.

Secretary SHALALA. Smaller businesses and individuals, those left who aren't part of these larger groups that are negotiating for discounts. There is no question that health care costs in the private sector are starting to slow down. But it is in large part because of the kind of clout big businesses have and because hospitals themselves under pressure are starting to slow down some of their growth.

There are efficiencies that are going on in the system, but we will not be able to take advantage of those or be able to do the kind of comprehensive health care reform we need to do if we start picking out segments.

Mr. MATSUI. Thank you.

I have no further questions, Mr. Chairman.

Chairman ARCHER. Mr. Camp.

Mr. CAMP. Thank you, Mr. Chairman.

Madam Secretary, in your testimony you mentioned with regard to the SSI program that the Inspector General found no evidence of coaching by parents. In testimony before this committee, we found that that is only part of the problem; that there are lack of audits, there is no accounting for how the money, the funds are spent, that they are even spent on behalf of the child for medication.

I guess I would like you to speak to that concern for a moment, if you would.

Secretary SHALALA. Well, the program was set up to provide flexibility to the family because each family, as you probably heard from testimony, has different needs, and a child with a different range of disabilities. So rather than bureaucrats determining specifically what the expenditures ought to be, the check is given to the guardian, to the family member to determine what is the best way to support the child.

That was the decision that was made. I think that—it had bipartisan support at the time—that we do not know a lot about specifically how the money is being spent except through our audits in these reviews that are going on.

But the intent I think was to support the family and the judgment of family members in terms of what was good for that child as opposed to government bureaucrats having a set of fixed rules about what the money could be spent on and then auditing that.

Mr. CAMP. The point I want to make is that even with the fact that there may or may not have been evidence of coaching by parents found by the Inspector General, there are a great number of concerns being raised if the children have a medical condition and the government has decided to give funds to the family for the medical condition of the child.

I think we have an interest in seeing that those funds are spent on behalf of the child's medical condition. I have another——

Secretary SHALALA. Mr. Camp, might I answer? We have zero tolerance. The fact that the Inspector General didn't find widespread coaching does not mean we have any tolerance for one child being coached and one person getting inappropriate funds.

Mr. CAMP. Good. Thank you. I am glad to hear that.

In your comments about the Supplemental Security Income program, you also didn't mention any reform involving drug addicts and alcoholics who are considered disabled and get monthly cash payments as well as other coverage, Medicaid. Should Federal taxpayers be paying money for chronic drug addicts?

Secretary SHALALA. We support the legislation that was passed last year by Congress which puts a time limit and insists on treatment for those that are drug abusers or have alcoholic problems—that the program be used as a transitional program for them while they are in treatment. The Social Security program—the Social Security agency is in the process of setting up that new system.

Mr. CAMP. Has the number of addicts receiving SSI benefits increased in the last few years?

Secretary SHALALA. Yes.

Mr. CAMP. Has that not been a rather dramatic increase?

Secretary SHALALA. The biggest increase has been children on the SSI program, as you know, because you have spent time worrying about the program. There has been an increase. Without the kind of tightness in terms of the fit with treatment programs and oversight that we really need to do, which the new legislation will strengthen our ability to do, the increases will continue.

Mr. CAMP. Thank you very much.

Secretary SHALALA. You are welcome, Congressman.

Mr. CAMP. I yield back the balance of my time.

Chairman ARCHER. Mr. Ramstad.

Mr. RAMSTAD. Thank you, Mr. Chairman, Madam Secretary.

I think you are fully aware of the importance of the medical device industry, not only to our health care delivery system but to our macroeconomy as well—$4 billion plus trade surpluses generated from the medical device industry, high quality jobs, and obviously a major contributing factor to the high quality of health care in the United States.

I am concerned about the user fee that is being imposed in the budget on these companies, without a commensurate guarantee that there will be any improvement in the medical device review process, which right now is literally driving hundreds and I daresay thousands—there has been at least one study that quantifies at least several thousand—jobs offshore.

Let me ask you this. Is the money that is allocated to the FDA, Food and Drug Administration, through the user fees imposed on medical device manufacturers a replacement of appropriate funds or an additional $24 million burden on the medical device industry?

Secretary SHALALA. It is additional money. If I might answer the issue of whether using user fees has produced results, in drug approvals, the user fee helped us to clean up 90 percent of the backlog, for example. In almost every case we have worked through with the appropriate industries what we intended to do with the user fees. In the drug user fee in particular, we had the support of the companies.

The medical device issue 1½ years ago when I first arrived was one of the first issues that was put on my plate by both the FDA Commissioner as well as by the community itself. All of us have to find a balance between making sure that we do appropriate reviews and making sure that they are done in a timely manner so that they don't have a negative economic impact on the companies that are involved.

That was also true on drugs being approved and other FDA approvals. To the extent these are resource issues, we have tried to address them and to streamline the process for approvals. We have new leadership—we have done a number of things—new leadership, new strategies, new resources to put in place to try to find that balance between safety for the American people and obviously the economic balance we are trying to achieve.

Mr. RAMSTAD. Madam Secretary, before my time expires, I have to ask a followup question. You said that 90 percent of the backlogs—you are talking about the 510(k) removal process or the PMAs have been cleared up at the FDA?

Secretary SHALALA. Of the backlog in drug approvals—let me check my notes. Not medical devices. I am talking about drugs, not medical devices.

Mr. RAMSTAD. I am talking about medical devices. My question is totally geared toward medical devices. I am talking about heart valves. I am talking about pumps and other——

Secretary SHALALA. No, I didn't say that about medical devices. My answer to the question was to say what the relationship has been in our experience. Our longest experience is on the drug side with the drug user fees.

Mr. RAMSTAD. I am talking about user fees imposed on medical device manufacturers. Is the money allocated to the FDA through user fees? Is this a replacement of appropriate funds or an additional $24 million on the medical device manufacturers?

Secretary SHALALA. It is additional, and it is to be used for streamlining the approval process for medical devices so we can reduce the amount of time that it takes for the approval process.

Mr. RAMSTAD. What is the quid pro quo? I mean, how do we know that the extra revenues will go to expedite the process?

Secretary SHALALA. My view is that we ought to be able to demonstrate that. This is a public budget, and you ought to haul us in and have us explain exactly what we are doing with the money and how we are streamlining the process. We have testified on that on the drug side. If we go to the business community and say, we need a user fee, and with that user fee we are going to streamline the process and cut down the approval times and do everything we can simultaneously to maintain quality, we ought to be able to demonstrate that.

Mr. RAMSTAD. Would you agree that the performance standards should be built into statute?

Secretary SHALALA. In general, I think that we can discuss performance standards. We have been supportive of the use of performance standards and outcome measures. Whether you want to put them into the statute or you want us to lay them out for you, I think I would rather discuss it with you.

Mr. RAMSTAD. I see my time is up.

Secretary SHALALA. I mean, they ought to be reasonable. We have got to think through what kind of performance standards are reasonable given the level of what the investment is.

Mr. RAMSTAD. But certainly what is happening is now an outrage. The average time for 510(k) approval is 240 days compared to 90 days, what it is supposed to be. Just in the last month, I have talked to a medical device company that is building a plant in the Netherlands, one in France, one in Italy. Those are good jobs we are losing and it is all because of delays in the approval of medical devices. There has got to be some restoration of reasonableness to the process. We have got to expedite this process.

Secretary SHALALA. Congressman, that is what we have tried to do from the point at which we first got into office in relationship to the FDA as well as the SSI program. I mean, across the government in terms of my responsibilities, I have very little tolerance for long delays that are inappropriate, that are just a matter of us getting the resources and the leadership and the management systems in place.

You will get no argument from me about it, particularly when we go directly to an industry and make a pledge, that if you give us the resources, we are going to tie them directly to a new system and make them additive.

Mr. RAMSTAD. Thank you, Mr. Chairman.

Chairman ARCHER. The gentleman's time has expired.

Madam Secretary, I had told you when you came earlier this morning that I thought perhaps since your piece of the budget was a very small part, that we might complete this hearing within 1 hour. It is clear now that the members have a great interest in this small part of the budget. I need to ask you whether your schedule will permit you to stay until each member has a chance to inquire if they so wish.

Secretary SHALALA. I think that I ought to stay, Mr. Chairman. Being respectful to this committee and to your interest in the range of responsibilities that I am responsible for, I will stay.

Chairman ARCHER. Thank you.

Mrs. Kennelly will inquire.

Mr. Coyne.

Mr. COYNE. Thank you, Mr. Chairman.

Madam Secretary, I noticed in the President's budget that Medicare part B premiums are set at 25 percent of the program's cost. Is this going to have an adverse effect on low-income seniors?

Secretary SHALALA. No, actually the percentage comes down a little. That is about what most people believe are fair, the beneficiaries as well as the Congress.

So our sense is that that is a fair number.

Mr. COYNE. The question is, though, is it going to increase the cost to low-income seniors?

Secretary SHALALA. I think the answer is, it is probably $3 less per participant than the previous year. So it will not increase their costs.

Mr. COYNE. Thank you. I represent over 20 hospitals. How will the President's budget impact these institutions, particularly the teaching hospitals?

Secretary SHALALA. The graduate medical education is left intact in this budget. Obviously, as the health care system is squeezing down with the reorganization of the private health care system and the movement of participants to HMOs, there is some impact on the academic teaching institutions.

This budget also has what I believe is a very generous increase in the National Institutes of Health, concerning the fact that we have straight-lined almost every other program in our budget. A 4-percent increase in NIH obviously impacts in a favorable way on the great teaching and research institutions in your district.

But I have been very candid with the academic health institutions in this country that they themselves are going to have to go through some changes to adjust to this much more competitive world, both for the private sector as well as from the public sector, and most of the institutions are going through those changes.

Mr. COYNE. Thank you very much.

Chairman ARCHER. Mr. Zimmer.

Mr. ZIMMER. Thank you, Mr. Chairman.

Madam Secretary, do I understand the administration's position correctly when I say that major cuts in Medicare will not be acceptable to you for funding tax cuts or for reducing the deficit? Major cuts in Medicare, and by cuts, of course, we mean reductions in the growth of Medicare, are acceptable to this administration only in the context of the kind of sweeping health care reform that a Democratic Congress refused to approve last year.

Secretary SHALALA. Let me sort out the two issues. Cuts in Medicare are not acceptable to us to support tax cuts. We did do some and we have always believed that comprehensive health care reform is what is needed to hold down the deficit and in fact reduce the deficit.

So within the context of more comprehensive health care reform—and the President has asked that we be able to sit down and to start taking the first steps toward comprehensive health care reform—that is the context in which we wish to discuss any changes in the Medicare program.

Mr. ZIMMER. What do you mean by comprehensive health care reform?

Secretary SHALALA. The President has suggested in his State of the Union speech and in his transmission of the budget to Congress that we start by discussing those things that we have some consensus on. Some insurance reforms that we discussed, long-term care issues, expanding coverage to children, perhaps, first, as a way of starting to reduce the number of people who have no health insurance that use the most expensive parts of the health insurance system, and providing more fairness to those and more flexibility for families who now use—may use a very expensive part of institutionalized care and may well want an alternative to keep their loved ones at home.

So there is a list of issues that we very much would like to discuss, and within the context of a discussion of moving toward everyone in this country having access to good and adequate health insurance, we are prepared to discuss the Medicare program.

Mr. ZIMMER. Do you have any specific numbers in terms of how much any of those incremental reforms are going to reduce expenditures in Medicare?

Secretary SHALALA. We presented a comprehensive plan last year in which we presented one option. Many Republicans as well as Democrats had other approaches which impacted on the Medicare program. What the President is committed to is a bipartisan approach. Have we changed our strategy? Yes. Are we backing away from health care reform? No. But we would like to sit down with you and look at options and look at their impact and what effect they may have on helping us slow down the growth in the Medicare and the Medicaid program.

Mr. ZIMMER. Is it not true that the Congressional Budget Office last year estimated that the administration's health care plan would increase the deficit rather than decrease it?

Secretary SHALALA. I think there were some findings that it would have some initial effects. But the point that we are making now is, let us sit down, not take just the President's model that he presented last year, but let's sit down at the table and talk about your ideas and our ideas and see where we can go. What we have argued is that it is hard to pull this down without having an impact on the private sector.

What we don't want to do is to start bludgeoning down the Medicare and Medicaid populations, putting at risk very vulnerable populations, and then shift the cost onto small businesses and middle-sized businesses, and individuals. What we would like to do is to sit down and look and see what we can do that would slow down the growth in the government programs, help to get some cost containment in the private sector, expand coverage, and help families deal with their long-term cost. But rather than our coming in with a rigid proposal, we have lots of computer runs and technical assistance that we can offer. Let's sit down and see what we can do, and that will help all of us to slow down the growth of health care in this country.

Mr. ZIMMER. Do you believe it is possible to balance the budget without applying some savings from Medicare to deficit reduction?

Secretary SHALALA. We do not believe that it is possible to reduce the deficit significantly in this country and to keep it down without doing something about the growth of health care in this country, and that requires a comprehensive strategy, taking steps this year and steps next year and steps the year after that.

Mr. ZIMMER. I know my time is up. Could you answer my question? Do you believe it is possible to eliminate the budget deficit without applying savings from Medicare to deficit reduction?

Secretary SHALALA. We do not believe that it is possible to reduce the deficit significantly and to keep it down in this country without comprehensive health care reform, working with—in a bipartisan way—with this Congress. The deficit will continue to grow—the government's own costs will continue to grow—unless we take a comprehensive approach. That is what we are prepared to do. We don't come to this with rigid ideas. We are prepared to sit and listen to what ideas you all may have.

Mr. ZIMMER. Thank you, Mr. Chairman.

Chairman ARCHER. Mr. Levin.

Mr. LEVIN. Thank you.

The private sector costs were less for the first time in Medicare, right, in previous years? Just review quickly, so we all understand it, as I understand it, Medicare costs in previous years went up less than the private sector?

Secretary SHALALA. They did.

Mr. LEVIN. This is a reversal, right?

Secretary SHALALA. Yes.

Mr. LEVIN. Some have suggested that we might save some money in Medicare and still further, Medicaid, by essentially requiring all beneficiaries to be in a managed care program, requiring it. Your position on that is——

Secretary SHALALA. We have been committed to choice for Medicare recipients. We believe that that choice ought to include HMOs, and we do not believe that people should be shoved into HMOs as a way of reducing the budget.

We also believe as the managed care industry does, that there has been a history in this government on at least two other occasions of trying to shift people perhaps too quickly and not thoughtfully into managed care as a way of reducing the budget. Neither of those efforts was very successful.

This is—the population for Medicare, the population for Medicaid—a vulnerable population, including disabled people. Some parts of it are very high cost. Whether managed care is a solution for everyone, whether people ought to have choices—we are very committed to choices. It ought to be—the whole business of laying out choices and giving people opportunities—ought to be done very thoughtfully and very carefully.

We are working with the industry. If you brought up here the people that represent the industry, they would say, this administration is working with the industry to think through how we array those choices and how we provide very good health care for people.

Mr. LEVIN. Let me pick up Mr. Zimmer's question, because I think it is important that everybody understand the administration's position. It is true, last year there were proposed cuts in Medicare, substantial cuts, as part of a larger comprehensive health care reform.

Some of us bore some considerable heat for supporting these cuts as part of an overall approach.

Give us an example of why it is relevant to look at the whole picture as we look at the major cuts to providers.

Secretary SHALALA. If we cut one part of the health care system, our experience is that we cost shift on the other part of the health care system. That was the standard operating conclusion of people who study the health care business in this country.

But it is compounded now by a slowing down of health care costs for some part of the private sector. The large corporations have been able to negotiate discounts in the system to protect themselves and their workers, leaving the rest of the market, smaller businesses and individuals, who would get caught if we started to squeeze down unilaterally, independent of a more comprehensive approach.

In addition to that, there are 1 million people that lost health insurance last year. For them, anything that started to squeeze down costs without simultaneously providing them access to the health care market would cause them to continue using the most expensive part of the health care market, many of them, the emergency rooms. So we have changes going on in the system that are not helped by simply pulling down on a small part of the health care system.

Mr. LEVIN. Thank you.

Chairman ARCHER. Madam Secretary, I did not contemplate inquiring, but I really would like to jump in on this issue. The bill that the administration supported and that came out of this committee last year for health care reform, if I remember correctly, included a cut of Medicare and Medicaid in the amount of $490 billion over 10 years. I believe that is an accurate number. It was supported by the administration and came out virtually on a straight party line vote out of this committee.

I am not sure I understand how you can take that much money out of Medicare and Medicaid, even if it is part of an overall health reform program, without shifting costs onto the other parts of health care. If there are ways to efficiently administer Medicare and Medicaid so that that does not become a shift cost, even as a part of overall health reform, then it seems to me that we ought to be working very diligently right now to implement those irrespective of whether we do health reform or not. Because, unless those cuts in the proposal that came out of this committee were the result of efficiencies in the delivery of health care through the Medicare and the Medicaid system, they still will shift cost over to the other elements of health care.

I would appreciate your comments on that.

Secretary SHALALA. You will remember that the President's bill had a number of elements to it, including holding down the costs in the private sector and having universal coverage so that there were not individuals without insurance coverage. So there were a couple of different things that went on in the President's bill, that is, everyone eventually got insurance. The private sector was able to hold down its costs because there were recommendations to control growth on that side. The public sector at the same time was bringing down its costs.

So it was the comprehensive nature of comprehensive coverage for everyone and holding down both private and public sector costs that slowed down the growth. Everybody has been talking about slowing down the growth in the public sector programs.

Chairman ARCHER. I understand that, but if you are going to take that massive amount out of Medicare and Medicaid, other than through efficiencies in the delivery of the care, it must be shifted on to the rest of the health care population. It makes no difference whether you do it by itself or whether you do it in conjunction with overall health reform.

I am not really sure that you responded to that inquiry. But I do hope that if there are efficiencies that can be brought to bear to reduce the costs of both the increases in costs in Medicare and Medicaid, that we would receive that in the way of proposals. Otherwise, whether we do it in the context of overall health care reform or we do it independently, it is going to cost shift to somebody else.

Secretary SHALALA. Mr. Chairman, I understand your point. I think the point that I was making is that one of the most efficient things we can do is to move people who have no health insurance out of emergency rooms into prevention programs. One of the other things we can do is expand the prevention programs and get some discipline—individual discipline in terms of how they use the health care system. So that is comprehensive—these programs now pick up with extra payments some of those additional costs.

There is no question that we are trying to introduce efficiencies into the system at the same time.

Chairman ARCHER. I can understand how that would apply to Medicaid, but not to Medicare. I don't think that there is a big problem with senior citizens using emergency rooms, nor is there a big problem relative to preventive health care in the Medicare population.

We are going to have to break and vote, and then we will come back immediately, and I appreciate your willingness to stay on with us.

Thank you very much.

[Recess.]

Mr. JOHNSON of Texas [presiding]. I will recognize myself. If you don't mind, I will ask you a couple of questions, Madam Secretary.

Your budget request is $716 billion. That is 7.5 percent, I am told, over the 1995 budget. The discretionary program's budget is about $37 billion, an increase of $1.5 billion, 4 percent over last year. Yet you keep talking about cuts and consolidations, yet you keep asking for more.

Can you tell me why you are asking for an increase?

Secretary SHALALA. Some of the President's key investments are part of the discretionary program, Congressman Johnson. That includes an increase in the Head Start program of $400 million, targeted specifically to improving the quality of the Head Start program, and a new initiative for zero to three that will allow communities across the country to fit in an earlier childhood program with their Head Start program, and to move the Head Start program to a full-time, full-year program so it will be supportive of low-income working families.

The National Institutes of Health also receives a $400-plus million increase, specifically for basic science research in cancer and AIDS, and in the Human Genome project. So a big chunk of that increase is Head Start, and the research program, plus an increase in this Nation's commitment to addressing drug addiction.

I had a question before on SSI. We need drug slots so that addicts receiving SSI get into treatment programs. So there are just a handful of targeted programs receiving increases. The rest either come down or we flatten out. But in addition to that, as I indicated, we consolidate the 104 public health service programs into a smaller number.

The community health centers in your community, which now apply for eight separate grants, will have one application, and it will be simple and straightforward, so that we cut out levels of bureaucracy. We reduce our personnel by the end of this century by 12 percent in the Department of Health and Human Services.

There are lots of things going on, but there are in fact new investments.

Mr. JOHNSON of Texas. I am told those consolidations don't result in any savings.

Secretary SHALALA. Some of them do and some of them don't. They result in savings, not in the money that goes directly to your community health center, they result in savings on the administrative side, in administrative costs. So we are eliminating positions, layers of positions, including some of our administrative costs in the regional areas.

So we are trying to protect the money that goes to citizens and reduce the amount of bureaucracy that gets that money there.

Mr. JOHNSON of Texas. Well, it seems to me, you talk about reductions in Medicare, for example, and I think Mr. Archer asked the question earlier, there were large reductions in that program forecast, though, and yet you are saying that costs are down to somewhere around 9.9 percent, and yet you are asking for I believe it is an 11.7-percent increase in the Medicare funding; is that true?

Secretary SHALALA. Well, what you are seeing is these costs go down over time, and we are projecting what we think the Medicare cost increase will be based on new populations coming in.

All of that, including the lower estimates, are reflected there in our actuarial statements.

Mr. JOHNSON of Texas. You are saying the costs are lower but you are asking for more money, so you don't expect costs to stay low; is that true?

Secretary SHALALA. The point I have made, Congressman Johnson, is what we are all trying to do is manage down the increases in these programs that we expect as new populations are added. Congress, in its wisdom, expanded the Medicaid program to very young children of low-income working parents, for example. So there will be new populations added to these programs. Also, as the country grays, we will have more elderly coming into the program.

What we are demonstrating, though, very much with the help of Congress on the Medicaid side, with management changes on the Medicare side, and with what is happening in the economy, as a result of taking big bites out of the deficit as well as other changes that are going to be happening in the economy, we are able now for the first time to show that the growth is slowing down. It is not slowing down enough.

That is why comprehensive health care reform very much has to be on the table this year and part of the discussion.

Mr. JOHNSON of Texas. I agree with you and I hope we can do it together. But you still have an increase in that program with a decrease in cost.

Let me ask you one other question. You have got $2.7 million in the budget for health care reform data analysis. I think that is the staff for the President's health care reform bill. As I recall, we are still fighting over some of the secret committee and secret deals that they made.

Why do you need this money?

Secretary SHALALA. There is nothing in our budget that doesn't support existing health care programs and the Department's own capacity to analyze data so that we can tell both the private sector as well as the managers in the public sector what is going on in the system, and our staff is very much focused on outcomes measures, setting up performance standards in the new kind of quality assurance systems.

Mr. JOHNSON of Texas. What does HCFA do?

Secretary SHALALA. We have policy staffs that are doing the theoretical work in quality assurance under the Public Health Service, that are analyzing low-income populations. HCFA has a database and in fact in this budget, as well as in the reinvention of government proposal, RIGO II, that we will present, we are rationalizing our database to make sure that we are collecting data that are useful in managing the programs and in exploring the impact of health care decisions in this country.

We would be happy to lay out that budget in some detail for you.

Mr. JOHNSON of Texas. Thank you. I appreciate that.

Mr. Christensen will inquire.

Mr. CHRISTENSEN. Thank you, Mr. Chairman.

Ms. Shalala, we appreciate your testimony today. Over the last several years, when Republican presidents submitted a budget to the Hill, it was always dead on arrival. It never got any kind of consideration. This year, President Clinton submitted a budget and we are looking forward to working with him, although it probably didn't go as far as we would liked to have seen.

I heard Congressman Steve Horn say yesterday that it is a different kind of DOA, devoid of accountability. You are asking us to do a lot of the heavy lifting in these areas. I think the budget is noticeably absent of entitlement reform.

Where I come from, in Omaha, Nebr., a cut means spending less than you spent the year before. In the 4 weeks that I have been here, I see that in Clinton-speak, a cut means a decrease in the increase. I think if there was ever a time that the American people are wanting to see this budget and this deficit and this debt come under control, it is now.

President Clinton's budget adds about $1 trillion to the debt. You said earlier you would be ready within 1 hour to sit down with us in a bipartisan fashion.

I am hoping that you have some specifics. You have mentioned a couple. Yesterday we heard from Senator Kerrey and another panelist about some specifics. Congressman Johnson talked earlier about some closed-door meetings and some things that maybe went on that didn't make it into the budget.

Do you have any suggestions, any specific ideas that we can look to that you might be able to work with us on in terms of transforming Medicare?

Secretary SHALALA. We have indicated both in my testimony as well as in the President's own budget report that we are prepared to sit down on a bipartisan basis and discuss specifics. But not simply to bludgeon down the Medicare and Medicaid programs, the most vulnerable populations we have in our society, but to look overall at health care costs in this country and at health care growth and not to shift additional costs on to State and local governments and on to individuals.

What we have said all along is that we believe that these growing health care programs cannot be brought under control until we have an overall strategy for health care costs in this country. That is the only point that I have been trying to make.

Do we have specifics? Yes. We laid them out in detail last year. They were rejected. Do we have alternatives to those? We would like to talk about those, too. Are we ready to sit down? We have experts sitting behind me that are ready to meet within the hour to discuss comprehensive health care reform.

Mr. CHRISTENSEN. Senator Kerrey mentioned yesterday about adjusting the CPI. How does the administration feel about that?

Secretary SHALALA. I think Mrs. Rivlin has expressed some reservations about that. It is more appropriate for her to talk about whether we should use something like an adjustment as opposed to what the President would prefer to do, and that is to get some genuine discipline into health care cost containment in this country, and that involves a comprehensive approach.

We believe that by cutting spending, which we are doing, by reducing the number of Federal employees, as we are doing, by getting the kind of deficit reductions that we got in our first year budget and which we continue to get in this budget, that way the government ought both to reduce the deficit now as well as get long-term deficit reduction through comprehensive health care reform.

Mr. CHRISTENSEN. Well, Madam Secretary, I think we are both headed in the same direction. One of us wants to get there a little quicker than the other. We hope we can work together on this.

Secretary SHALALA. Thank you, Congressman.

Mr. JOHNSON of Texas. The time of the gentleman has expired. Mr. Cardin will inquire.

Mr. CARDIN. Thank you, Mr. Chairman.

I would like to follow up on Mr. Archer's point about the package that was submitted last year, which contained significant savings in Medicare and Medicaid, as Mr. Archer pointed out. But if memory serves me correctly, the lion's share of those savings were used to finance comprehensive health care reform, in order to expand the number of people who would have a rational way to pay for their health care services, to give us the ability to have everyone covered by health insurance, and to institute discipline in health care costs in both the private and public sector.

Wasn't that the whole strategy of the plan and why you could get savings if you can have parity and reduction in health care costs across the board rather than picking on the elderly and the Medicare system?

Secretary SHALALA. Exactly, Congressman Cardin. We do not believe that simply bludgeoning the Medicare and Medicaid programs will produce anything other than our populations, the elderly, the disabled, young, having less health care and being far more vulnerable. Nor will it take care of the problem of millions of Americans who don't now have health insurance. One million last year, most of whom were working, having lost access to health insurance. It really does require a comprehensive approach.

Mr. CARDIN. In response to Mr. Christensen, we were ready to act last year and move last year, and we have lost a year, and I regret that. We are not going to be able to enact a 1995 comprehensive health care reform bill that will deal with universal coverage and the effect of cost containment. That is not going to happen, unfortunately, in 1995. So I applaud you for coming forward with some steps that I think can help us to move toward the goal of universal coverage, and to bring down health care costs which will ensure savings to Medicare and Medicaid.

Let me just mention a couple of those areas. If I heard you correctly, you granted a lot of State waivers. So you are going to permit at least States to move forward. If we are not able to at the national level, States can come forward with some constructive approaches to reduce cost and expand access. The administration is prepared to work with the States?

Secretary SHALALA. We are.

Mr. CARDIN. Good. Let me give you the figure. I always like to brag about the Maryland system. The statistics indicate that for this year the cost for Maryland hospital care rose slower than the national growth rate, saving our State and the Federal taxpayers additional moneys. The States are prepared to move forward, and I hope that we will continue to work in that direction.

Choice, I think, is an excellent suggestion, to give the elderly additional options, to allow the elderly to choose what type of health care plan they would like to be in, and save us some money and still protect the program for the elderly. I think that is another concrete way that we can move forward to save some money, and I am glad to see the administration is prepared to move in that direction.

I want to follow up on Mr. Coyne's thoughts on graduate medical education. One of the issues that we were working on in a bipartisan basis last year was to try to share some of the cost of our academic medical centers. I agree with you, our academic centers have to be more efficient than they have in the past. All medical facilities are going to have to be more efficient than they were in the past.

But it is not fair to ask an academic medical center to recoup all of its cost through a competitive rate structure when it has to compete with hospitals that don't have the same type of cost.

Medicare—government has been prepared to help our academic centers; the private sector has not. I would hope that one of the ways we may want to look at correcting that would be to provide a system where all payers or users of the health care system contribute fairly to the extra cost associated with academic health centers.

I see by your nod that you would be prepared to work with us to try to develop that type of a proposal?

Secretary SHALALA. Absolutely, Congressman. As you have pointed out, the academic health centers do have extra costs. They treat a population that is very high cost. They are in the process of training the next generation of health professionals. That costs more. I think that there are multiple functions that have to be recognized as part of an overall comprehensive health care reform effort.

Mr. CARDIN. I thank you for being here and I thank the willingness of the administration to look at all these issues, to work with this Congress to move forward as far as we can in 1995 on health care reform. We are not going to accomplish everything we want to, but it would be a shame if we don't take advantage of this opportunity to work in a bipartisan basis to achieve some health care reform.

Mr. JOHNSON of Texas. I thank the gentleman.

The chair recognizes Mr. Collins to inquire.

Mr. COLLINS. Thank you, Mr. Chairman.

Thank you, Madam Secretary. In the district I represent, hospitals constantly tell me that they are having to shift costs primarily because of reductions in reimbursements to providers. Reimbursements were reduced in the 1993 tax reform. Would that not have resulted in additional cost shifting by providers to those who are insured by private sector insurance?

Secretary SHALALA. I think the point I was trying to make, Congressman Collins, is the way to avoid cost shifting is to avoid just making cuts in one part of the system as opposed to making certain that we have coverage for everyone, because what happens to a health care provider, to a hospital, for example, is if we keep squeezing them down on the public programs, then they have to squeeze down on their coverage, for example, of services they offer to people that are uninsured. Or they have to shift, if we inappropriately squeeze down on this side, they have to shift their costs to the insurance plans of those who do pay.

So what we are not anxious to do is to simply squeeze down on the public pieces without having a comprehensive plan and taking some steps toward coverage, toward insurance reform, and doing some things with the Governors to give them more flexibility to handle their costs on Medicaid. If everybody—if we move toward everyone getting coverage, then the health care providers who are very committed to high quality care in this country can better manage the resources.

Mr. COLLINS. I understand because you have said this about 10 times already to different——

Secretary SHALALA. I think 23.

Mr. COLLINS. For 23 times. I didn't take my shoes off, so I can only count to 10. But the point, too, is that any time you have a reduction in reimbursements, not only do you have a tendency to shift costs, but you also have a tendency to reduce services that could be or may be provided to seniors who are insured under the Medicare insurance program. Also, President Clinton's comprehensive health care plan contained a provision that would have determined what was necessary and appropriate when it came to providing health care services.

So in a sense, reduction and reimbursements can lead to means testing of services to seniors who are covered under the insurance program. Is that not true?

Secretary SHALALA. Well, it could lead to a number of things that I would not like to pinpoint what Congress may do if we are trying to reduce costs under the Medicare program.

I also think that, to be fair, there also are efficiencies that can be built into the system. While health care providers want to tell us about their need to reduce service if we cut down their resource, they have also made an effort to get more efficient in terms of the delivery of services.

So it is always a combination of things. What we have to do is be very careful we are not shifting the costs and eliminating participation from the health care system in the United States by doing something that is reckless.

Mr. COLLINS. But you do agree, then, that one of those tendencies could be to means test services or determine what is appropriate.

Secretary SHALALA. It certainly has always been on the list of what people have told us they will do if we recklessly start reducing the programs. But it certainly is not something I would recommend.

Mr. COLLINS. One other question, before my time runs out. A lot has been said about those who are covered under Medicare insurance who are in higher incomes, $90,000, $100,000, and up. What would be the administration's position, or does the administration have a position on increasing the premium cost to those who are of higher income versus reduction of reimbursements?

Secretary SHALALA. In the past we have made some recommendations, but only in the context of health care reform. Again, we have in this budget committed ourselves to having those part B premiums at about 25 percent of the cost. We think that is about right.

Again, any changes in the Medicare program we are suggesting would be discussed within the context of health care reform. So I can't answer specific questions about what would we do if, except in the context of health care reform. That is 24.

Mr. COLLINS. I didn't use an if. I just said does the administration have a position on increasing the premium cost to the higher income versus reduction in reimbursements.

Secretary SHALALA. Our position is a negative one, and again, let me repeat that all of these issues have to be done within the context of a broader discussion about health care reform. What we want is a fairer system, not adding to the financial burdens of our most disabled and most senior citizens.

You don't want to do that any more than I do. So I just can't answer a specific question about a piece except in the context of health care reform. So the answer would be no, if it was independent of—but we would be happy to discuss a number of things in the context of health care reform.

Mr. JOHNSON of Texas. The time of the gentleman has expired. Mr. Ford will inquire.

Mr. FORD. Thank you very much, Mr. Chairman.

Madam Secretary, the administration deserves high praise in proposing increases in Head Start, early childhood programs that you talked about earlier, breast cancer research, along with AIDS research. The administration does not leave those programs which place the largest burden on HHS untouched.

Some of my Republican colleagues have suggested block granting many of these proposals as the answer to many of the problems.

Let's talk about the Medicaid program. We talked about a 9-percent increase. The Republicans are saying with flexibility give the Medicaid program in a block grant to the States and cap it at about 5 percent.

What is the administration's position on the Medicaid block grant program?

Secretary SHALALA. We have been happy to discuss with individual States flexibility in the use of their Medicaid program. We have some serious reservations about moving programs that have very vulnerable populations to a situation where we would cost shift to the States a much higher burden, which is essentially what some of the discussion of block grants is suggesting.

The populations in Medicaid are children and mothers and heavily—the costs are heavily related to the disability population and to the frail elderly population. So what we ought to do is to take a position that these vulnerable populations are ones which this country has a longtime commitment to protect. We ought not to be deep in discussions about limiting resources so that the States get higher burdens themselves in any way for helping these populations.

Mr. FORD. Are you witnessing the impact of some of the waivers you have given to the States?

Secretary SHALALA. We have tried to be very careful and all of those waivers have had to be budget neutral. As you know, your own State of Tennessee, what it has tried to do is take the existing expenditures on Medicaid and add some things and tried to cover more people, some low-income working people, putting people into a managed care situation.

Mr. FORD. Overall, it has been a pretty good program, but I am wondering whether they are running into financial problems.

Secretary SHALALA. I think we want to watch it very carefully. The new Governor has had some concerns about this. I have talked to him myself. We are at the beginning of that program. While they have overcome some huge obstacles, we want to work with the State to make sure that none of the populations, who the citizens of this country care deeply about, are adversely affected by these decisions.

Mr. FORD. Madam Secretary, let me change the subject a little bit. Can you tell me what the status of the disability backlog is today? Some of my colleagues on the other side of the aisle brought the issue up earlier. I would like to follow through on some of the questions here.

Secretary SHALALA. We have committed ourselves to reducing the disability backlog. The Social Security program in the eighties went through radical reductions in the number of employees, from about 80,000 to 60,000.

Mr. FORD. So that was about a 20-percent cut in the staff?

Secretary SHALALA. That was about a 20-percent cut.

Mr. FORD. That was under the Reagan administration.

Secretary SHALALA. Exactly. Simultaneously, the rules of who was eligible for the programs changed the numbers in terms of who was coming on to the programs. We produced a huge backlog. We have put together what is called reengineering——

Mr. FORD. The backlog started back a decade ago in the eighties or more, and we have not been able to catch up on that backlog.

Secretary SHALALA. We have not been able to catch up, and one of the things that this administration pledged itself to is to develop a strategy for bringing down the backlog, and for processing claims considerably faster. To do that, we had to rethink with our employees the entire disability process, trying to find out where the glitches were in the system.

W now have a strategy that we believe will cut down on the number of days it takes for the initial disability decisions and help us reduce the number of pending claims. It has been a painful process.

Mr. FORD. Are you seeing a significant growth in claims since about 1988?

Secretary SHALALA. We have, and that is a result of children coming into the SSI program and to some extent some of the alcohol and drug addicts coming into the program, but particularly children coming into the program. It has overloaded the Social Security program, which of course was operating with significantly fewer employees.

But we have thought it through, we have some new resources, we have got the strategy, and it will start coming down. But it is very tough to do when you are dealing with very vulnerable people.

Mr. FORD. Some of my colleagues on the other side of the aisle are suggesting we cut all children off SSI in order to get to the root of the problem rather than just trying to go after those who defraud and abuse the system.

Do you have any suggestions what we should do in this area?

Secretary SHALALA. First of all, cutting all the children off would be a national tragedy. There are children in this program that are disabled and who have a very low income who need help. What we have done, though, is recognize that there may be some problems with the program, and there are two activities that are going on.

First, Congress in its wisdom made some changes in SSI in relationship to drug and alcohol addicts. It is now going to be a more temporary program that puts people into treatment programs.

Second, the Congress in the Social Security independent agency bill asked me by January to appoint a commission to take a look at the children's issue in disability. I appointed former Congressman Jim Slattery of Kansas to head that commission. They have already had their first meeting. The first thing I told them at the meeting was that they were out of time, that Congress needed their advice as soon as possible, and I pleaded with them not to take the whole year. But I think that Mr. Slattery will be up to talk to many of you.

Finally, the administration itself has its own internal review of all of our disability programs headed by the OMB Director, the domestic policy director, and me, reviewing all of the disability programs in the administration.

Mr. JOHNSON of Texas. I thank the gentleman. His time has expired.

I would like to note we love children too, and we are not about to take any programs away from them indiscriminately. I don't know of the proposal that you are talking about, Mr. Ford.

Mr. FORD. Mr. Chairman, I am only making reference to the welfare reform package that the Republicans keep talking about with all of the—many of the problems that we witnessed with some of the abuse and fraud with SSI. But I think many of your colleagues on the Republican side are in fact suggesting that in order to address the problem, that we do away with the supplemental security income of all children who are now receiving it.

Those who abuse it should be cut from the program, but it is a very responsive program to the needs of disabled children in this country, and we on the Democratic side of the aisle want to make sure that we keep it intact.

Mr. JOHNSON of Texas. I hope you do.

The chair recognizes Mr. Hancock to inquire.

Mr. HANCOCK. Well, I would like to respond also to the gentleman from Tennessee. I don't know of any recommendation on our side of the aisle to completely eliminate helping children or getting rid of the SSI to protect children. If it has been mentioned, I haven't heard it, and I think I have heard just about the most conservative reductions in government proposals that are submitted to any congressional office.

I would like to just make a comment rather than ask a question, or maybe the Secretary can explain it. The largest percentage increase in the President's proposed budget is the judiciary. I realize that that is a very small part of the overall budget. It is not going to balance the budget.

But I would just like to make the comment that a lot of us in the private sector are pretty consistently or pretty regularly concerned about the growth and the money that we are spending primarily for the purpose of protecting government rather than spending the money to protect the citizens.

I think that is what some of the crime bill is all about. I mean, we want to spend more money, we want to solve the crime problem. But it would appear that some of the money that we are spending in the judiciary isn't to solve the problems of the citizens, it is to protect government from their own citizens. I would just like to make that observation.

You may or may not want to make a comment on it, but if we are going to take a look at the growth of government, let's take a look at where the most rapid growth is, and the most rapid growth in this budget is in the judiciary.

Secretary SHALALA. I probably should take a pass on this. I am responsible for 44 percent of the budget, but not the judiciary.

But let me say that the President recognizes the very serious growth in health care costs in this country, and we are obviously anxious to bring down those costs. In this case what we are trying to do is protect very vulnerable populations.

The growth in the judiciary, in crime costs, to the extent that it is related to our ability to get our values straight, is part of the discussion that we are having here—a broader discussion about how we treat our vulnerable citizens and what kind of opportunities we offer in this country, so that we reduce the number of people that end up using—particularly the criminal parts of—the judiciary system.

So you obviously are entitled to your views, and I respect your right to exercise them, but whatever our feelings about the judiciary, our commitments, and our values about children and about the elderly and the disabled ought to be kept firmly in mind as we work through a very large part of the government's commitment.

Mr. JOHNSON of Texas. Thank you, Secretary Shalala.

Mr. Rangel will inquire.

Mr. RANGEL. Thank you.

Welcome, Madam Secretary. You and the President have done a wonderful job in working toward reduction of the deficit in a way that doesn't pain people. I think it would have been a more tremendous job if we didn't have this middle-class tax cut. But that is another issue.

My concern has always been provisions for the treatment of drug addicts. While it appears, though, the war against drugs has been declared over and that we don't see any Member of any Cabinet position stressing the importance of dealing with this problem, and it costs us hundreds of billions of dollars in terms of crime and health expenses and productivity, and I assume that in your budget the treatment provisions have been expanded.

Secretary SHALALA. They have, sir.

Mr. RANGEL. What bothers me is that there never seems to be a connection between treatment, so-called rehabilitation, and job training, and jobs. I have told Secretary Reich that every program that I have seen, not every, but most, that is funded, it is funded by the States, because we give them more flexibility, they are closer to the problem, we can't have the Federal Government interfering with these things, and the States not only make assignments politically, but the same drug addicts are going in and out of the programs.

There is no training. There is no education. So you come out with self-esteem and you are drug free and you are unemployable. Nothing seems to change over 20 years. Could you respond?

Secretary SHALALA. I share your view that the programs have to be connected in a way that we don't concentrate just on getting someone drug or alcohol free without the connection to job training and other kinds of programs. Let me give you—well, one of the examples you know very well. In Harlem we are working very hard on an empowerment zone that will try to make these connections.

In the crime bill, the prevention part of the crime bill, the importance of it is the way in which we work with the young person right through into that employment. In Oregon we are embarked upon an experiment with the State to connect Federal programs with State and local commitments so that there is a seamless approach to youth, to children, so that the job connections are done.

In the welfare reform bill we have done the same thing, so that education is in there as well as the connection to the job and staying in the job.

Mr. RANGEL. That brings me to my next question. First of all, in the welfare reform bill we are working off of the Contract With America. So I don't know what is going to be in there. In the crime bill, the majority is trying to remove those preventive measures that were placed in it.

Is there a White House or Cabinet team that would give a theme to all of the inner cities or all of the areas that are connected, that takes us from the rehabilitation center to placing someone back in the job market?

Secretary SHALALA. There is a team at the Cabinet level as well as at the sub-Cabinet level. I have assigned our regional directors, one of whom is with me here today, Lynn Yeakel, who is from Philadelphia and represents that region, to work almost full time with those empowerment zones to make sure we bring not only the resources that are committed to the empowerment zones, but it is really the connection with the rest of the resources—the State programs with Federal programs—there really is a seamless connection.

Mr. RANGEL. We have a group, we don't know what to call ourselves because it is not here what the new rules will allow us to do, Members of Congress, Republicans and Democrats, that are concerned about this issue, that sit on the various committees that have jurisdiction, and we would hope that your team member that works with the Cabinet, we could ask Lee Brown whether he could put together a team too, so that no matter what legislative committee has jurisdiction, we will be able to work more closely with you.

Secretary SHALALA. Exactly. We are looking at our administrative requirements, too, to make sure we don't produce things under our control that would impede the connections between the programs.

Mr. RANGEL. Thank you, Madam Secretary.

Mr. JOHNSON of Texas. I thank the gentleman.

The chair recognizes Mr. McDermott to inquire.

Mr. MCDERMOTT. Thank you, Mr. Chairman.

During the 1994 elections, the Republicans bragged all over the country and took great pleasure in announcing that they killed health care reform. It seems today from listening to their questions that they really are upset at you for not coming up here with a budget that cut the daylights out of Medicare and Medicaid, as though it was now your responsibility to come up with the proposal on health care.

I think there are some of us on this committee who applaud you for not putting up big cuts in Medicare and Medicaid for deficit reduction, but rather holding it back to be used as a part of a comprehensive reform. I think that it is incumbent on the other side at this point to come forward.

The President rightly put this on the agenda and said if we don't have health care reform, we will not get deficit reduction. Now, my mother and her sisters, one in Detroit, one in Dallas, one in Seattle, they watch this and they can't understand sometimes what the connection is between health care reform and deficit reduction.

I would like you to take the rest of my time explaining what the connection really is so that people understand what this whole debate is really all about.

Secretary SHALALA. What the debate is really about is that some people have health insurance in this country and others don't. Unless everybody has health insurance, adequate, high-quality health insurance, then some of us will pay more than others. Any time we try to fix the system by cutting down the costs on the government program, we will shift some of the cost to those who have health insurance. They will pay more money. The people who have no health insurance won't have a chance to get any health insurance.

So it really is a question of how we are going to keep our budget with some kind of discipline and reduce the deficit. We cannot reduce the deficit in this country until everybody has good health insurance and access to health insurance.

We can't do it by bludgeoning the programs for the elderly and for children and for the disabled, because that will only shift the costs on to State and local governments, on to hospitals, and they will pass on those costs to private people who pay for health insurance.

So I think the answer to your mother is, we are all in this together, and each of us must make a contribution. The government—and the government programs have to make sure that they are well managed and that they don't spend more than is necessary. The private sector has to do everything it can to cover its workers.

All of us must work together to make sure that those who get up in the morning and go to work—after all, they are left out of the system—have coverage, or the system will be expensive because the people without coverage will put off their health care or they will walk into an emergency room for their health care.

So the answer really is that we cannot reduce the deficit, we can't get anywhere near getting a budget that is anywhere near balanced, unless we get everyone covered, and we all work on the efficiencies ourselves and together.

Mr. McDERMOTT. Let me carry that a little further, because I listened very carefully to the Republicans, looking for some hope that there might be some thought over there about doing something about health care. The Speaker has talked about getting rid of Medicare and giving my mother a medicheck kind of voucher saying, no longer are we going to do it through the Medicare system, you are going to take that check and buy from an insurance company.

Now, is my mother going to be better off with that sort of situation where she goes and buys a private insurance program than what she presently has under Medicare today? Would you recommend that to her?

Secretary SHALALA. No, I wouldn't recommend it to her. For a number of reasons. She is part of a segment of our population that is at higher risk in terms of health care. One of the reasons that the government got into this in the first place was because the private health insurance system in 1965 only actually covered half the elderly population.

Now only 1 percent doesn't have coverage. The private insurance market, while it has begun to move to offer HMOs, for example, to the elderly, want people that are as healthy as possible because of their costs.

Mr. McDERMOTT. So they are risk selecting?

Secretary SHALALA. They are risk selecting and they admit that they are risk selecting. One of the reasons they are doing that is because they can't absorb the cost of the higher risk populations without increasing their premiums.

So——

Mr. McDERMOTT. So you are really saying that any senior who has any problem would be worse off with a voucher system where they had to go into the private system than they are under the present system.

Secretary SHALALA. One of the reasons the President said let's take some steps, we need insurance reform, is that most seniors will have a preexisting condition. Being senior is a preexisting condition. So simply giving people vouchers and expecting the market to respond to a high risk population—it is not just seniors on Medicare, as you well know, or on Medicaid. It is disabled people. There is not a private sector market that will absorb all of the most disabled people in our society.

The private sector very much wants to work with the government. They administer the Medicare program. I think they do a pretty good job. Together we are going to make even more reforms. But they also want their risk protected from high risk populations, and the government's role is very much to do that.

That doesn't mean we should be paying more for healthy people than the private sector. But it does mean that we have to share the risk and share the responsibility and find a public-private partnership.

What we learned the last time around, it seems to me, Congressman McDermott, is that we have a mature private health care system in this country, that whatever reform needs to take place can't take place just on the government's piece. It has to be a partnership between the private and the public sectors, thoughtfully closing this huge gap of people that have no access to health insurance, thoughtfully getting more efficiency into the system, and that we shouldn't be bludgeoning down the public sector's health care programs for vulnerable people as a way of trying to deal with health care costs or reducing the President.

Mr. McDERMOTT. I hope you will tell the President to hang in there and force the other side to put up or shut up.

Mr. JOHNSON of Texas. The time of the gentleman has expired.

In defense of the Speaker's comments on medicheck, let me indicate he was looking for choice and that is one of the options available. I think the Secretary would agree that—in fact, you made the statement earlier that you wanted the elderly to have a choice, and in health care the same thing applies.

So thank you for your comments in that regard.

Mr. Payne will inquire.

Mr. PAYNE. Thank you very much, Mr. Chairman.

Thank you, Madam Secretary. Since this is a budget hearing, I had questions about numbers. These are numbers that I think are really good news in terms of the presentation you have made. Specifically those that are on the chart that is still here, talking about the Medicare and Medicaid growth slowing. I think you said in your presentation that we can look at some $212 billion in deficit reduction that has occurred as a result of the slowing of the growth of Medicare and Medicaid.

Specifically, in your testimony you mention that Medicaid has been reduced from 13.9 percent growth to an 8.7 or 5.2 percent, which is a very substantial amount of growth. Medicare, from 11.9

to 9.9 percent, or has been lowered by some 2 percent over the course of the last 2 years as we project forward.

You then went on to say that Medicaid last year had experienced a 63-percent increase in the number of Americans enrolled in managed care, and that there had been a lesser, I think a 16-percent increase in individuals on Medicare into managed care.

I guess my question then has to do with these facts and these figures. Are you suggesting that there is a direct correlation between those people who are going into managed care programs and the ability to limit the growth of cost of the Medicare and Medicaid programs?

Second, what other significant factors would you attribute this lessening of the rate of growth to? Because it could be helpful to us as we look forward policywise.

Secretary SHALALA. Let me make two points about the Medicaid program. First, the dramatic effects of the 1991 provider tax restrictions, removing the creative financing that States have been doing to try to leverage more Medicaid money. That was a bipartisan bill. I have acknowledged that, and all of us together ought to take credit for pulling down some of the growth in the Medicaid program.

Second, the use of waivers by States, moving some of the populations into managed care. In the process of those negotiations, those waivers have a contract, often 5 years, that is budget neutral, which means that we are getting some discipline from the States as part of our negotiations with them, which is holding down some of the costs over a period of time, the term of these waivers.

While we are saving money, the States are saving some money, which is what they were up to, by moving some people to managed care, and we are saving it because those waivers had to be budget neutral. I think that the court is still out on the issue of how much managed care for vulnerable populations saves us money.

Certainly with children, where you have managed care that has a big investment in prevention, immunization, prenatal care, perinatal care—all of us can see in our heads that we are going to save money if we make those early investments.

For very disabled people, whether managed care will work for them or a very specialized kind of group, for the elderly where we have choices, we know there is some risk selection. There are wonderful stories which I think indicate high intelligence on the part of managed care, their recruiting efforts at health resorts, where large numbers of elderly are to find healthy elderly to put into managed care.

There is some risk selection going on. You can't blame them for doing that. The issue is, are people in Medicare satisfied. It is a new generational experience. My generation is much more used to managed care than some previous generations. So I think in Medicaid, there are actually two things, two significant things going on. One is the law that was passed, and the other is these contracts, these managed care contracts and the way they have played out. They said I have learned my lesson well.

Mr. PAYNE. I see my time is almost up. I had some other questions. What I will do is submit those in writing.

Secretary SHALALA. I would be happy to handle them or come see you, whatever.

Mr. PAYNE. Thank you very much.

[The information follows:]

QUESTIONS FROM MR. PAYNE

1. What has been primarily responsible for this reduction in growth?

- In 1993, this Administration worked successfully with the Congress to enact the largest deficit reduction bill in history;

- Successful implementation of regulations following the bipartisan passage of the 1991 provider taxes and donations act has had a significant effect toward limiting Medicaid DSH payments and states' use of creative financing mechanisms which increase Federal payments;

- Aggressive program management, such as replacing five under-performing Medicare contractors and redoubling our efforts to combat fraud and abuse in the Medicare and Medicaid programs;

- A slow-down in both general and health care inflation reduces the rate of spending growth.

2. To what extent has the increased use of managed care in the Medicare and Medicaid programs contributed to this reduction? What percentage of the Medicaid population is currently enrolled in managed care? of the Medicare population?

- It is not clear to what extent managed care has contributed to the reduction in Medicare and Medicaid spending.

- In the Medicare program currently, differences in enrollee health status between managed care and the general Medicare program have hindered out efforts to achieve savings. We have attempted to make adjustments to our payment rates to account for these differences between the populations.

- To help ensure that future growth in Medicare managed care produces savings, we are exploring methods such as competitive bidding for risk contracts, as well as improving our health status adjusters.

- In the Medicaid program, studies have generally found that managed care only produces a one-time savings of about 5 percent to 15 percent over baseline costs without slowing the rate of growth.

- Twenty-three percent of the Medicaid population, or about 7.8 million people, is enrolled in managed care. About 9 percent of the Medicare population is enrolled in managed care, which is 3.1 million beneficiaries.

3. What should be the target growth rate for federal health care spending: CPI, CPI plus growth in population, the rate of private medical inflation, etc.?

- In the President's Health Security Act, the target rate of growth for overall health spending was CPI four years after the bill was enacted. However, I believe that rate of growth is achievable only if we reform the entire health care system.

4. What is the anticipated rate of growth for long-term care in the Medicaid program? acute care? care for the disabled?

- Medicaid long-term care services are projected to grow at an average annual rate of less than 8 percent from 1996 through 2000. Within that overall growth rate, institutional long-term care is expected to grow at an average annual rate of 7 percent while community based long-term care is projected to grow at almost 11 percent.

- Acute care services are projected to grow at an 11 percent average annual rate between 1996 and 2000.

- The cost of Medicaid services for the disabled are expected to increase at an average annual rate of almost 10 percent from 1996 through 2000.

5. What are the fastest growing costs/programs in Medicare and Medicaid?

- In the Medicare program, based on projected expenditure growth for the FY 1996-2000 period, Part B expenditures are projected to outface Part A expenditures. Within Part B, the fastest growing areas are: outpatient hospitals, independent labs, and group practices.

- In the Medicaid program, acute care services are the fastest growing component. The costs of acute care services are projected to increase an at average annual rate of 11 percent from 1996 through 2000. While prescription drugs represent the bulk (over 40 percent) of acute care services costs, clinic and health center costs (25 percent of acute care costs) are the primary drivers of the rate of increase. These costs are projected to grow at an average annual rate of over 14 percent.

6. What should be done to bring down the rate of growth in the future in order to save additional federal funds?

- I believe we must be more aggressive in combating waste, fraud, and abuse.

- We must explore ways to manage the program more efficiently, and give beneficiaries more options than they presently have to receive their health care.

- Reform to the overall health care system would also have a significant impact on reducing costs.

- I want to work with the Congress in a bipartisan manner to find ways to control the growth in the Medicare and Medicaid programs.

Mr. JOHNSON of Texas. Thank you very much, Mr. Payne.

The chair recognizes Mr. Lewis to inquire.

Mr. LEWIS. Thank you, Mr. Chairman. Thank you, Madam Secretary.

Madam Secretary, I think it is possible for us to remember that we did a lot of heavy lifting, the Democrats for President Clinton, and led the way on deficit reduction during the past 2 years. It was not an easy vote, but we did it. I hear from some of my colleagues this morning that the sinners have become the preachers. I think it is about time for the Republicans to do some of the lifting. I think we all would appreciate it.

Madam Secretary, I don't want you to respond to that, that was just a little editorial.

Madam Secretary, the administration has been at the forefront on welfare reform. Last year you introduced a welfare reform bill proposal. This year you have pledged to build upon your budget proposal by working with Congress to reform welfare. I commend you for your hard work and for your leadership in this area.

You have been keeping your eyes on the prize. I agree that welfare reform should focus on moving those on welfare into the work force. We must provide the necessary training, education, child care, and health care. Unfortunately, many of my colleagues on the other side, many of the Republican efforts at welfare reform appear to focus less on work and more on morality.

It creates paternalism, not opportunity. I fear that as you work with Congress, you will be—I hope this is only a fear, Madam Secretary—but that you will be influenced by this attempt to legislate morality. Will you comment on whether your efforts to reform welfare will emphasize work or Federal micromanagement of people's lives.

Secretary SHALALA. It will indeed, and frankly we believe that the President's proposal reflects the values in our larger society. It moves people from welfare to work. It has time limits. It holds both parents responsible, including the establishment of paternity and child support enforcement. We have been working with the committee. We still have some disagreements.

We would like to put more emphasis on the family, for example, than on the bureaucracy. We have disagreements about what happens to a young child born to an unwed mother, and disagree sharply on whether those children should be denied cash assistance for their entire lives.

In addition to that, we believe that young people who make the decision to have the child ought to stay at home, and that their parent ought to get some assistance if they stay at home, as opposed to putting the money in the bureaucracy and letting the bureaucracy make a decision. In many ways, my response is the same as with the SSI. I think we have to hold parents responsible. I think that is moral and reflects values.

We did put forward a welfare reform plan. We have been discussing our ideas with the committee. I am sure there is more debate ahead, not only in the subcommittee in the next few days, but also in the larger committee as well as in the House and then in the Senate. But we intend to hold to our standards, and that is that we ought to have welfare reform.

Simply shifting the responsibility from one bureaucracy to another is not welfare reform. Reducing the amount of money the States get for welfare reform is not welfare reform. It is simply cost shifting. Not putting education and training into place and real job opportunities is not welfare reform, it is simply reducing the rolls by throwing people off of welfare.

So we bring both values as well as strong views that we think are reflected in many of the experiments that have gone on and the work that has been done by Governors and by county officials over the years, and by those of us who have spent our lives working with populations that are very vulnerable.

Mr. LEWIS. Thank you very much, Madam Secretary. I look forward to working with you.

Secretary SHALALA. Thank you.

Mr. LEWIS. Thank you, Mr. Chairman.

Mr. JOHNSON of Texas. Thank you, Mr. Lewis.

Madam Secretary, I want to thank you for being so gracious to accept inquiry from all sides up and down the spectrum and for extending your time with us this morning. Thank you so much. We hope to see you again.

The committee stands adjourned.

[Whereupon, at 12:25 p.m., the hearing was adjourned and reconvened on Thursday, February 9, 1995, at 10 a.m.]

PRESIDENT'S FISCAL YEAR 1996 BUDGET

THURSDAY, FEBRUARY 9, 1995

HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
Washington, D.C.

The committee met, pursuant to call, at 10 a.m., in room 1100, Longworth House Office Building, Hon. Bill Archer (chairman of the committee) presiding.

Chairman ARCHER. The committee will come to order.

Mr. FORD. Mr. Chairman.

Chairman ARCHER. Mr. Ford.

Mr. FORD. Mr. Chairman, could I be recognized just for 1 minute, please? I would like to make an inquiry to the chairman, really.

Chairman ARCHER. Does the gentleman wish to make an opening statement today?

Mr. FORD. No, I would like to make an inquiry to the chairman on a different subject matter, Mr. Chairman.

I read this morning, Mr. Chairman, with great interest in the Washington Post, which described the welfare reform mark that Chairman Shaw is apparently announcing today before the Chamber of Commerce; and I would like to know, when will members of this committee receive copies of the mark on welfare reform, when will the Democratic members receive the Republican welfare reform package?

Our staff, Mr. Chairman, was told that a markup document would be delivered yesterday. Then they were told that it would be available today. Obviously, something is available that the Washington Post has printed and quoted Chairman Shaw on welfare reform. Why was the information given to the Washington Post; and the ranking minority member of the committee and Democratic members and other members of this committee, we have not received the welfare reform package?

You have repeated over and over, Mr. Chairman, that you wanted to be fair with the Democratic members of this committee, and I would urge the chairman of this committee to be fair with us, not let us read in the Washington Post what is going to be unveiled in the welfare reform package that we have waited on. I have asked Chairman Shaw over and over, when will we receive a copy of this document. It is insulting to us on this side of the aisle to read it in the Washington Post and not have a copy of it delivered to us when the chairman of this full committee has promised us and assured us that he wanted to be fair in these areas as we try to move to mark up many of these bills within the first 100 days, in keeping with what you have promised the American people.

Chairman ARCHER. The gentleman's comments are not in order relative to the business before the committee today. The gentleman should take his comments to the chairman of the Subcommittee on Human Resources.

This chairman will be fair, including listening to repeated derogatory remarks against the chairman himself, which occurred redundantly yesterday and were out of order under the rules of the House and the rules of this committee. This chairman has been more tolerant than any chairman that I can remember in many, many years in this committee. The markup document has been given earlier to the minority than was ever given to us during the time that you controlled this committee, and for any further comment on that, I would suggest that you go to the chairman of the subcommittee.

Mr. FORD. Mr. Chairman, I want you to know——

Chairman ARCHER. In fairness to our witness today and the announced proceedings of this committee, we will commence with the hearing.

Mr. FORD. Mr. Chairman, I wanted to say that I have great respect for you.

Chairman ARCHER. The gentleman is not recognized.

Mr. FORD. May I be recognized?

Chairman ARCHER. We will proceed with the agenda that was scheduled for the committee today.

Our witness today is Dr. Alice Rivlin, who is the Director of the OMB. We will continue to proceed with our hearings on the President's budget, which we believe should be given serious consideration by the Congress—and not declared dead on arrival as our predecessors did, because we believe that there are many elements of it about which we can work together.

We do believe that our Nation is at a fiscal crossroads, and I know that Dr. Rivlin over the years has been very much of a deficit hawk. Yet we see in the President's budget continued deficits as far as the eye can see of $200—perhaps $300 billion a year. The public is demanding a smaller and smaller deficit, however, and not continued deficits that go out into the future.

Congress has its responsibility in this regard, and we would like to work together with the administration in doing all that we can to downsize government and reduce spending in the years ahead with a commitment to get to a balanced budget. As has been the custom of the committee through this hearing process so far, I will yield to Mr. Coyne for the opening statement of the minority.

Mr. COYNE. Thank you, Mr. Chairman.

Dr. Rivlin, I want to thank you for appearing before the committee here today. Your expertise on budget issues is highly respected in this country, and we always profit from your testimony before the committee. I also want to commend you for all your efforts in producing the administration's fiscal year 1996 budget proposal. We all realize how much work it takes to put together a comprehensive plan like this, and your competent, dedicated service is greatly appreciated.

I also want to commend the administration for its past budget recommendations to the Congress. Over the last 2 years, the administration has brought a degree of fiscal responsibility to the budget that was sorely needed by this country. I am sure that you, more than most people, appreciate the fact that the 1993 deficit reduction package represented a lot of tough decisions and sacrifice. The payoff, however, has been well worth it. OBRA 1993 reduced Federal deficits between 1994 and 1998 by more than $500 billion from what they otherwise would have been.

Tuesday in your testimony before the House Budget Committee you mentioned that the latest estimates indicate that the deficit reduction package we passed in 1993 will cut over $600 billion from Federal spending by 1998. That accomplishment should not be taken lightly. As a result of this responsible stewardship, economic growth in 1994 and 1995 has been very strong and unemployment has dropped to its lowest level since 1990.

I think that we must recognize the Clinton administration's past efforts at deficit reduction when we consider your new budget submission this year. OBRA 1993 wasn't the administration's only contribution to deficit reduction, either. We must also remember that the Clinton administration took the lead on deficit reduction last year when it proposed its health care reform plan to the Nation. The Clinton administration recognized that in order to achieve a sustainable budget in the long run, runaway health care costs have to be restrained. Since Congress chose to reject the administration's proposal, it is incumbent upon this body to propose a different solution to the problem.

The same is true of welfare reform, I might add. I suspect, however, that the American people, as well as some Members of Congress, don't yet have a clear understanding of the pain and sacrifice that lie ahead if we expect to achieve and maintain a balanced budget after the year 2000. With that concern in mind, I think that this committee should be very cautious about any decisions it makes to enact sweeping tax cuts this year. We should make certain that any tax cuts we do enact meet the most demanding criteria. Paying for tax cuts will require cutting or eliminating a great many existing programs, and let's not kid ourselves that all of the necessary cuts will come from eliminating waste, fraud, and abuse. That just won't happen. We will have to cut programs that really do make people's lives better. We had better be sure that the benefits of these tax cuts outweigh the benefits from the programs we are cutting.

By the same token, we had better make sure that these tax cuts are designed to address our Nation's most pressing problems. Is making life better for families that do have a roof over their heads a more pressing need than reducing the number of homeless families in the Nation? Is investment in new equipment more important than investment in our children's education?

It seems to me that our mission is to find the proper delicate balance between competing worthy goals. There is no easy answer. In short, any tax cuts we must enact should meet the test of providing substantial, tangible benefits to this Nation, and they should do so without placing additional burdens on the most vulnerable members of our society.

Dr. Rivlin, you have been an ardent advocate of fiscal responsibility. I hope that I have placed your presentation today in its proper context, and I thank you for appearing before us today. I look forward to hearing your testimony.

Ms. RIVLIN. Thank you.

Chairman ARCHER. Dr. Rivlin, welcome to the committee. I think you are aware of our rules. We will be pleased to hear your verbal testimony. Should you wish to submit something of greater length, without objection, it will be entered into the record. You may proceed.

[The prepared statement follows:]

STATEMENT OF HON. JIM RAMSTAD

Mr. Chairman, thank you for giving us the opportunity to question Director Rivlin this morning.

Like many of my colleagues, I am extremely disappointed in the President's recently released budget. At the same time, I think it is important to commend Dr. Rivlin for her efforts to inject a sense of urgency about the deficit in the administration's internal dicussions of this matter.

Last Saturday's article about the President's budget described Dr. Rivlin as the sole administration advocate for strong deficit reduction measures. While I don't share Dr. Rivlin's desire to cut Social Security or raise taxes on the already overtaxed American public, I am deeply concerned about the Federal deficit and the President's fiscal year 1996 budget.

Mr. Chairman, thanks again for calling this hearing. I look forward to hearing Dr. Rivlin's testimony and to exploring in greater depth this important issue.

STATEMENT OF HON. ALICE M. RIVLIN, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET

Ms. RIVLIN. Thank you, Mr. Chairman. I would like to submit a longer statement, and I will briefly summarize it so that we have plenty of time for questions.

I am pleased to be back before this committee and to have an opportunity to participate in the opening stages of the dialog about the 1996 budget. I look forward, as does the administration, to working with this committee—not only on the budget, which is the subject for today, but on other parts of our mutual agenda. We especially look forward to working with the committee on health care and welfare reform. While these parts of our mutual agenda are not in the budget we are talking about today, they are very important priorities of the administration on which we look forward to working with you.

The administration has worked hard on this budget, and as Mr. Coyne says, it is not easy to make a budget. We believe that it is a good budget and that it continues our work on the goals we have held for the last 2 years.

A major theme of this budget is raising living standards for average Americans, both now and in the future. This has been a major element of the Clinton administration's economic strategy. From the start, the Clinton administration has emphasized deficit reduction and, at the same time, investments in people, technology, and infrastructure so we can have a more productive, higher wage economy in the future. This budget continues the fight for higher wages and better lives for average Americans. It does it in several ways.

We are proposing a tax cut, not for upper income Americans, but for working families with children under 13, young families who are having a hard time making ends meet. We are proposing that education and training be made more available and more affordable to average Americans. We believe that increased education and training is the key to better jobs in the future; that theme runs throughout the budget. You see it in our tax proposals, with the education and training deduction. You see it in our proposal for broadening the individual retirement account and making it possible for more people to participate, save, and use those funds, penalty free, for a broader range of nonretirement purposes (for example, education, extraordinary medical expenses, and the purchase of a first home). You see it in our proposal for a GI bill for American workers. We believe this proposal sends an important signal to American workers about the Federal Government's willingness to help them get the skills they need for better jobs.

In the GI bill we are proposing that we pull together a plethora of training programs already on the books, thereby creating a pot of money for skill scholarships for dislocated and low-income workers and giving States increased flexibility to provide services their workers need.

Although this budget cuts severely in other places, it invests in Head Start, WIC, the School-to-Work Program, Goals 2000, and science and technology programs. We believe these programs will raise productivity and wages in the future.

This budget also continues our commitment to fiscal responsibility. We cannot be faulted for not caring about that.

The deficit was out of control when we came into office. In fiscal year 1992, the deficit was the highest it has ever been. It was $290 billion and headed up. That was an unsustainable situation. The use of the Nation's saving on an escalating basis to finance the government, as opposed to productive investment, was the greatest threat to future living standards. This threat caused us to put forth a great deal of effort on deficit reduction in the first few days of our administration. We got a deficit reduction plan up here in 17 days. It was a plan for 505 billion dollars' worth of deficit reduction over 5 years, about half spending cuts and half revenue increases.

The Congress worked hard on our plan, modified some of it, and by a bare majority had the courage to vote for it in each House. It took effect and has been enormously successful. Since the plan was put into place, it has actually worked better than we thought. We now estimate that the effects of the deficit reduction plan on cutting the deficit will total about $616 billion cumulatively over the 5 years to which it applied.

This deficit reduction package has produced a rapidly growing economy. We are even in the pleasant situation of having to worry about whether it is growing too rapidly. That is much better than 2 years ago when we were worried about stagnation and whether there would be a recovery. We have created almost 6 million jobs. Things also look good on all the statistical fronts—little inflation, high growth, and a very successful economic picture.

This budget contains more deficit reduction measures. There is a total of $144 billion in budget savings, of which we propose to use $63 billion over 5 years to fund provisions of the Middle-Class Bill of Rights. Most of the cuts, $101 billion of the $144 billion, are in discretionary spending. Others are mandatory.

We are not proposing any tax increases in this budget. Although we have emphasized cutting discretionary spending, we do not believe in slashing government indiscriminately. We believe that we must all work together to have a leaner, more effective government.

A government that works better is the second theme that animates this budget. This, too, has been a continuous emphasis of the Clinton administration from the beginning, with the Vice President's leading of the National Performance Review. This budget accelerates the Vice President's work by detailing plans for aggressive restructuring at the Departments of Transportation, Energy, Housing and Urban Development, along with the General Services Administration and the Office of Personnel Management.

We have 131 programs that we are proposing to terminate. Most importantly, we are proposing to consolidate 271 programs into 27 performance partnerships. Performance partnerships, we believe, are a new addition not only to the lexicon of talking about government, but to concepts of how the Federal Government, States, and localities should work together. It is not just a new name for block grant. We believe that the Federal Government, the States, and in some cases, localities must work together to decide what the grants are supposed to produce. Why are we doing this? How can it be measured? What results do we want? When we have agreed on the answers to these questions, the Federal Government should allow the State or locality to get results in the way that seems best adapted to their conditions. It is not just a grant for States and localities to use the money any way they want; results have to be there for all to see.

The Vice President likes to talk about trust and accountability. We trust the States and localities to use the money well, but we must all be accountable to Federal, State, and local taxpayers.

The final theme that runs through this budget is that of American leadership. We want a leaner, more effective government, not just in the domestic arena, but in the international arena as well.

The budget emphasizes the quality of life in the military, which Secretary Perry has been emphasizing, and the importance of force readiness. In December we announced an addition of $25 billion over 5 years to the defense budget, which we believe will give us a more ready and modern force. It brings on line modernization at the end of the decade—supports initiatives that Secretary Perry is taking to attract and retain the best young people for our armed services.

In conclusion, Mr. Chairman, I am very happy to be here and look forward to working with the committee, not only on the budget, but also on welfare and health care reform, which we believe to be key to future deficit reduction.

We did not put our health care reform proposals in this budget. There are no Medicare cuts in this budget because we do not believe Medicare cuts should be used for tax cuts; but we want to work with this committee and other committees of jurisdiction as we consider health care reform, including the reform of Medicare and Medicaid. I believe all of us have an opportunity, Mr. Chairman, to work together and fashion a budget and a program for this government that is fiscally responsible, preserves and strengthens the activities people need from their government, and eliminates or changes those activities that are not working well.

It is a hard job, and we want to work together with you.

[The prepared statement follows:]

TESTIMONY OF
ALICE M. RIVLIN
DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET
BEFORE THE
HOUSE COMMITTEE ON WAYS AND MEANS

FEBRUARY 9, 1995

Mr. Chairman, members of the Committee, thank you for inviting me to offer the Administration's views on the President's fiscal 1996 budget. For the third straight year, the President has proposed a detailed plan to create a smaller, more effective Government for average Americans -- that is, to help create his "New Covenant" between the Government and the American people.

Executive Summary

The President proposes to build upon his strong record of achievement. With the help of his economic plan, which Congress passed in 1993, the President helped to jump-start a weak recovery. The result was lower interest rates, little inflation, and the creation of more than 5.6 million new jobs.

With a plan that called for a record $505 billion in deficit reduction over five years, and has in fact produced over $600 billion in deficit reduction, the President has reduced the deficit from $290 billion in 1992 to $203 billion in 1994. We expect the deficit to be under $200 billion this year. By 1998, the deficit will fall to its lowest level as a percentage of GDP since 1979.

At the same time, the President has made great progress in reinventing Government through the National Performance Review. We have reduced the workforce by 102,000 positions while streamlining departments and agencies, cutting red tape, and providing better service.

Now, we plan to go further. The President has proposed $144 billion of budget savings -- $63 billion to finance the middle class tax cut that I will discuss in a moment and $81 billion to reduce the deficit further over the next five years. As part of those savings, he proposes to terminate 130 programs and consolidate 271 others into 27 new "performance partnerships."

Not everyone has shared in the economic recovery. As a result, the President proposes a Middle Class Bill of Rights, which will cut taxes for middle-income Americans and give unemployed or dislocated workers grants to purchase the job training they need.

He also is continuing to reduce the Federal bureaucracy and will, by the end of this decade, cut it to its smallest size since John Kennedy was President. As part of Phase II of the National Performance Review, he has proposed to restructure the Departments of Housing and Urban Development, Energy, and Transportation, the General Services Administration, and the Office of Personnel Management.

In the coming months, also as part of Phase II, the President will examine every other program and activity to determine which to terminate, which to restructure, and which to shift to the States, localities, or private sector.

Major Themes

This budget revolves around three major themes -- themes that have dominated the President's economic strategy for the past two years.

1. Raising the standard of living for average families, now and in the future: The President is proposing a Middle Class Bill of Rights. For the short term, it will provide needed tax relief to help millions of average families raise their living standards now. And for the long term, it will give those families the tools they need to raise their living standards in the future.

The Middle Class Bill of Rights:

* Provides a $500 per child tax credit for middle-income families with children under 13;

* Expands eligibility for Individual Retirement Accounts (IRAs) and allows families to make penalty-free withdrawals for a range of educational, housing, or medical needs;

* Offers a tax deduction for the costs of college, university, or vocational education; and

* Creates a G.I. Bill for America's Workers by consolidating 70 job training programs and using the money to offer "Skill grants" through which dislocated and low-income workers can choose and pay for the training they need to find new and better jobs.

The President proposes to build upon his investments in human and physical capital -- investments that will help to raise national productivity and, in turn, living standards for the future. Overall, he proposes to increase investment spending by $9.7 billion in fiscal 1996 over 1995.

The G.I. Bill for America's Workers is a new element of his continuing agenda for improving the education and skills of America's workers, enabling them to compete for high-wage jobs in the new economy. In the last two years, the Administration has enacted the Goals 2000 bill to encourage States and localities to reform their educational systems; revamped the student loan program to make post-secondary education affordable to more Americans, and pushed successfully for the School-to-Work program that enables young Americans to move more easily from high school to training or more education.

In this budget, the President proposes a 10 percent increase for the Special Supplemental Feeding Program for Women, Infants, and Children (WIC), to $3.8 billion; an 11 percent increase for Head Start, to $3.9 billion, and an 86 percent increase for Goals 2000, to $750 million.

As you know, the President has proposed a complete overhaul of the welfare system. Under reform, welfare recipients would get the training they need to go to work. By helping low-income families help themselves, reform would mean greater self-sufficiency for these families.

The President's bill embodied certain key principles: time limits on AFDC for parents who can work, and job placement assistance and training for those who need them; greater State flexibility to experiment with innovative programs that aim to increase self-sufficiency; strict parental responsibility requirements to ensure that both parents support their families; a national campaign to emphasize to teens that they should delay childbearing until they can adequately provide for their children; and a commitment that welfare reform must not increase the federal deficit.

This year, the Administration will work on a bipartisan basis with the new Congress to enact fundamental welfare reform -- the kind that embodies the principles listed above.

The President's budget also emphasizes investments in science and technology to improve future productivity and U.S. competitiveness in the new economy. It proposes a 13 percent increase for the Defense Department's core Technology Reinvestment Project (TRP), to $500 million; a 4 percent increase for biomedical research at the National Institutes of Health, to $11.8 billion; a 20 percent increase for the Commerce Department's National Institute of Standards and Technology, to a total of $1 billion; and a 4 percent increase for the National Science Foundation, to $3.4 billion. The President seeks to strengthen the Administration's coordinated efforts to promote science and technology through the National Science and Technology Council and to improve the payment system for federally-sponsored research at colleges and universities.

The budget also continues the Administration's strong commitment to deficit reduction. When we arrived, the deficit was a clear threat to future living standards. It was projected to rise from $290 billion in 1992 to more than $300 billion immediately, and then to near $400 billion a few years down the road. The deficit was absorbing a huge share of national saving that could otherwise be spent on the kinds of investments that increase productivity.

Working with Congress in 1993, we enacted a five-year budget plan designed to reduce the deficit by a cumulative $505 billion from 1994 to 1998. Because the economy has performed better than expectations, we now expect to generate $616 billion in deficit reduction over that time. The deficit measured $203 billion in 1994 -- a huge drop from the $290 billion of two years earlier. Except for an anomaly in 1997, we expect it to remain below $200 billion for the rest of this decade.

More importantly, we have reduced the deficit from 4.9 per cent of Gross Domestic Product (GDP) when we arrived to a projected 2.7 percent this year. Clearly, we have brought the deficit under control.

But we are not satisfied. In this budget, we propose to reduce the deficit between 1996 and 2000 by another $81 billion. More importantly, our budget would bring the deficit down to 2.1 percent of GDP by the end of this decade -- its lowest level since 1979.

We are proposing $144 billion in new budget savings -- $63 billion to pay for our middle class tax cut and $81 billion for more deficit reduction.

How did we generate the $144 billion in savings?

Most of them, $101 billion, come in discretionary spending cuts. Of the $101 billion, $21 billion comes from Phase II of the Administration's effort to reinvent Government through the National Performance Review. This includes the restructurings of the Departments of Housing and Urban Development, Transportation, and Energy, the General Services Administration, and the Office of Personnel Management. The rest of the savings are outlined in the program-by-program detail in the budget for the years 1996-2000.

Also as part of Phase II, the Administration has begun an intensive effort to examine the other Federal departments and agencies to determine which functions and activities to continue, which to terminate, and which to shift to the States, localities, or the private sector. We anticipate that, through this effort, we will revise our five-year, program-by-program plan and offer proposals to restructure agencies in the same way that we have for those cited above.

The budget contains $29 billion of mandatory savings. Most of it comes from extending the Medicare and Veterans reforms of the 1990 and 1993 budget reconciliation acts, accelerating our successful direct student loan program, expanding the principle of user payment for the electromagnetic spectrum, and other smaller savings.

The budget also includes tax compliance savings of about $9 billion, including about $0.4 billion from reinventing Government.

Finally, the budget includes a small amount of savings that does not score for budgetary purposes, including net spending reduction from the Administration's non-emergency supplemental appropriation proposal for fiscal 1995, interest savings associated with the direct student loan program, and debt service savings from all of the other proposals. Partially offsetting these savings are bookkeeping costs due to personnel cuts; reducing the size of the Federal workforce means that the Federal Government and its employees make smaller contributions to the pension funds.

In sum, these proposals fully offset the tax cuts and leave enough additional savings to keep the deficit under control beyond the five-year budget window. While the economy is growing, the deficit is not.

2. **Projecting American Leadership:** Our funding proposals for international affairs, $21.2 billion, and national defense, $258.3 billion, support American leadership around the world. These two elements are synergistic: we design and prepare our forces and programs to support our national interests and foreign policy goals. Together, they create the foundation for our leadership. I will turn first to international affairs, then to national defense.

However critical to promoting our vital national interests, funds for international affairs programs and institutions constitute only 1 percent of our total budget, requiring that we carefully focus on their most effective use in supporting our most important goals and objectives.

Our budget promotes and defends our vital interests in regions that have long been central to our national security: Europe, the Middle East, and Asia. Our budget includes $788 million to support economic and democracy programs in the new independent states (NIS) of the former Soviet Union. In Central Europe, our budget supports the missions of supporting democracy, free markets, and peace by providing $480 million in funding to help healthy, market democracies emerge. The budget also maintains our long-standing support for the peace process in the Middle East, requesting more than $5.2 billion to assist countries participating in that process.

A strong and growing world economy that incorporates an increasing number of nations is essential to our own economic growth. Our budget provides increased support to strengthen our trade position in the global market and especially in Central Europe, Russia, and Ukraine through such agencies as the Export-Import Bank.

Our leadership is important to prevent and provide a humanitarian response to crises and conflicts that have so visibly divided many nations in recent years. Our budget supports this leadership effort by providing $1.7 billion for refugee, humanitarian feeding, and disaster assistance programs.

The Nation has built, and this Administration continues to support, a powerful military capability. Our defense budget, which is significantly higher than that of any other nation, supports one of the world's largest military forces, with a superior level of quality and talent. It continues our commitment to maintaining high levels of training and readiness of that force and to equipping it with a technology second to none.

In discretionary spending, the budget requests $258.3 billion in budget authority and $262.2 billion in outlays for the National Defense Function. The outlays represent 16 percent of all spending in the budget.

The Administration continues to place its highest priority on the readiness of U.S. defense forces -- ensuring their ability to mobilize, deploy, and operate effectively in the face of varied challenges of the post-Cold War era. The Defense Funding Initiative, providing $25 billion in higher spending from 1996 to 2001, supports our commitment to high levels of readiness, as does the requested defense supplemental appropriation for 1995. For 1996, the budget proposes funding of $91.9 billion for Operations and Maintenance, the principal readiness-related account.

This budget also contains several initiatives to improve the quality of military life: a 2.4 percent military pay raise and an increase in military community and family support, including more child care facilities, family counselors, and improved recreational facilities.

Superior technology is the hallmark of the U.S. armed forces. In particular, we expect investments in information technologies and sensors to give our forces major advantages in gathering, processing, and acting upon information from the battlefield. The budget proposes $7.8 billion for science and technology programs.

The budget also enables us to maintain stewardship over our nuclear capability. The budget proposes $11.2 billion in total Energy Department spending on defense activities. It includes $6.6 billion of cleanup and disposal of wastes from prior nuclear weapons activities, $0.7 billion for developing nuclear reactors for Naval vessels, and $0.7 billion for nonproliferation, arms control, and other activities.

Intelligence remains a critical ingredient of our national security posture. To support it, we propose to keep the Intelligence budget at the 1995 level. To plan for the future, the President and Congress established a commission of distinguished Americans that will spend the next year reviewing the roles and capabilities of the Intelligence Community. Their conclusions will help to guide future decisions on goals and resources.

Wise investments with dual-use technologies support national defense. They allow defense systems to draw on leading-edge commercial developments in such areas as computers and communications, and they allow investments in defense programs to accelerate commercial progress in such areas as advanced materials and space systems. The Administration's dual-use investment strategy focuses heavily on electronics and sensors. The Technology Reinvestment Program is a key component of this strategy. It awards Federal funds competitively, on a cost shared basis, to enable industry-led projects to create new dual-use technologies. Since the start of the TRP program in 1993, over 15,000 companies have submitted over 3,000 proposals to participate; the program has made over 250 awards. The budget requests $500 million for the TRP program.

The Defense Department's main challenge with its facilities is to tailor them to the downsized force structure. DOD is working to ensure that base closure and realignment decisions will generate a more efficient use of the remaining defense infrastructure. The budget provides $3.9 billion in 1996 to implement closure and realignment decisions. At the same time, DOD is committed to assisting the economic redevelopment of communities affected by base closures. In this effort, the budget increases funding for DOD's Office of Economic Adjustment (OEA) to $59 million, $20 million over 1995, to help Base Realignment and Closure Commission communities plan for economic redevelopment.

3. Making Government Work: The President is building on his initial success in making Government work and moving out in dramatic, new directions.

Through the National Performance Review (NPR), which the President created two years ago, the Administration has improved service to Government's "customers," cut red tape, empowered Federal employees, and eliminated programs that no longer serve a useful purpose. We have sought to ensure that Federal programs achieve real results -- e.g., cleaner air -- rather than merely spend taxpayer dollars.

We streamlined Federal agencies, cutting management layers and excessive controls. Already, we have reduced the workforce by 102,000 full-time equivalent (FTE) positions. Continuing the President's effort, the budget proposes 1.976 million FTE. By the end of 1996, the President will have cut FTE by 173,300, reducing the Federal Government to its smallest size in 30 years. He also will be nearly two-thirds of the way toward the required reduction of 272,900 by 1999, as outlined in last year's Federal Workforce Restructuring Act.

In its first phase, the NPR, under the direction of Vice President Gore, mostly examined the "how" of Government -- the human resource management, procurement rules, and other processes by which the Government operates. In general, it did not focus on the more basic question of "what" the Federal Government should, and should not, do.

With this budget, the President has begun to tackle this very fundamental question. He is proposing a major restructuring of three Cabinet departments -- Housing and Urban Development, Transportation, and Energy -- and two major agencies -- the General Services Administration and the Office of Personnel Management. We expect these restructurings to save $23 billion over the next five years.

We also are proposing to consolidate 271 programs into 27 "performance partnerships." In exchange for giving States, localities, and other providers more flexibility in how they spend Federal funds, we are seeking more accountability for that spending by focusing on actual performance. Rather than merely calculate the inputs of a program -- i.e., funding levels -- we are focusing on outputs -- what the programs actually accomplish.

The consolidated programs include 70 to create the G.I. Bill for America's Workers, mostly from the Departments of Education and Labor; 108 from the Public Health Service; 60 from the Department of Housing and Urban Development; 30 from the Department of Transportation; and three from the Department of Health and Human Services.

More importantly, these restructurings and consolidations are the first step in a Government-wide examination of departments and agencies, which the President has asked the Vice President to lead. This effort is designed to sort out responsibilities among the Federal, State, and local levels of government, and between Government and such private sector providers as businesses, non-profits, and community groups. Working with the NPR, OMB, the President's Management Council, and the White House policy councils, Federal agencies will examine every program, determine which to continue, which to eliminate, and which to shift to the States, localities, or private sector.

Program Detail

Restoring the American Community: American communities embody our sense of place, belonging, and togetherness -- the very security on which we depend. But our communities face the pressures of great challenges that threaten the ties that bind us together. Violence and drug related crime are tearing at our social fabric.

This budget would invest in our communities, by increasing funding for programs that help to strengthen our communities -- Americorps, empowerment zones, and the urban and rural economic development initiatives. It would continue to commitment undertaken in last year's crime bill, providing the funding necessary to continue making progress towards the goal of putting 100,000 police on the streets and providing increased funding for other crime control efforts.

Americorps: The 1996 budget proposes to increase funding for the President's national service initiative to $1.1 billion. This is a $290 million increase from the prior year, and would permit the expansion of the program to 47,000 participants. This would keep the program on the President's goal of reaching 100,000 participants over three years.

Empowerment Zones and Enterprise Communities: On December 23, the Administration designated nine Empowerment Zones and 95 Enterprise Communities, plus two additional urban enterprise zones. The Administration designated Atlanta, Baltimore, Chicago, Detroit, New York City, and Philadelphia/Camden as urban EZs, enabling each to receive $100 million in flexible block grants. We designated Kentucky Highlands, Mississippi's Mid-Delta Region, and Texas' Rio Grande Valley as rural EZs. Los Angeles and Cleveland were designated as supplemental urban EZs. The budget contains the funding necessary to continue these commitments.

Urban and Rural Economic Development: We propose $4.8 billion in 1996 to fund a new Community Opportunity Funds program to help local and State governments address the most critical needs of distressed communities. We also propose funding the Rural Development Initiative at a level of $5.8 billion to continue to support grants, loans and loan guarantees -- an increase of $716 million over the prior year.

Controlling Violent Crime and Drug Abuse: Our proposed $21.5 billion in discretionary spending in 1996 represents an increase of $3.4 billion from 1995 to fight violent crime. The largest share of the increase would go to help State and local law enforcement agencies.

Community policing: The President is committed to putting 100,000 cops on the streets, and this budget contains $1.9 billion in funding -- an increase of 45 percent from 1995. This additional funding will make significant progress toward meeting the goal, bringing the total number of new officers funded to over 40,000 by the end of 1996.

Crime Control: Overall, the level of funding for the Administration's major violent crime control initiatives increases from $2.4 billion in 1995 to $4.3 billion in this budget -- an increase of $1.9 billion.

Drug Control: Drug control spending will increase by $1.3 billion, from $13.3 billion in 1995 to $14.6 billion. The budget targets additional funding to treatment, prevention and education, and criminal justice.

Reforming the Nation's Immigration System: This budget reflects the Administration's continued commitment to controlling our Nation's borders and sharing the national burden of costs associated with illegal immigration.

Border Security Initiative: The budget includes $656 million in new funding to support the border security initiative. These funding increases will strengthen border control and management activities of the Immigration and Naturalization Service and the Customs Service, and strengthen enforcement through the INS and the Department of Labor to apprehend and deport illegal immigrants. The budget proposes to finance this initiative, in part, through a modest border services user fee.

Helping with the Costs of Illegal Immigration: The budget also contains an additional $370 million to assist States with particularly heavy burdens associated with illegal immigration. This increase is divided among three programs: State Criminal Alien Assistance Program; Medicaid discretionary grants to States; and the Immigrant Education Program.

Ensuring a Clean Environment: The Administration has developed several new approaches to advance the President's commitment that a healthy economy and a healthy environment go hand in hand. The budget targets spending to ensure that we make the Government a partner working with local citizens, not an overseer.

Ecosystem Management: Funding levels reflect the high priority that the Administration places in maintaining ecologically diverse and health environments along with economically viable communities -- $390 million to continue the Northwest Forest Plan; $99 million for the South Florida Ecosystem Restoration Initiative; and $70 million in joint Federal-State mandatory spending related to the Restoration of Prince William Sound.

Climate Change Action Plan: The budget proposes $336 million, an increase of $104 million -- 45 percent -- to fulfill the President's commitment to reduce greenhouse gas emissions to 1990 levels. This funding is designed to promote a public-private partnership rather than relying on command and control mandates.

Superfund: In each of the past three years, the Superfund program has cleaned up more sites than in its entire first decade. The budget proposes $1.8 billion for Superfund, a $332 million increase over 1995.

Investing in Science and Technology: Investing in science and technology is the key to assuring our Nation's economic well-being for generations to come. During the Cold War, most Federal spending on research and development (R&D) was defense-related. This research not only produced the most advanced military technology in the world, but the most technologically advanced economy in the world. Today we face a no less serious challenge that requires us to improve our competitiveness through a balanced mix of civilian and defense, public and private R&D.

NASA: The budget proposes $159 million to begin research to produce a reusable space vehicle. This continues our Nation's leadership in space exploration and, at the same time, expands the opportunities for a commercial space launch market.

ARPA/TRP: The Technology Reinvestment Project implements the Defense Department's dual use technology strategy -- a critical investment in transferring technology to commercial applications. The budget proposes $500 million for TRP in 1996, a 13 percent increase from 1995.

NIST: The Commerce Department's National Institute of Standards and Technology has two core programs -- the Advanced Technology Program (ATP) and Manufacturing Extension Partnerships (MEP). The budget proposes $491 million in 1996 for ATP, $60 million more than 1995, and $147 million for MEP, a $56 million increase from 1995.

NIH: Proposed funding for biomedical research is $11.8 billion, a $468 million increase from 1995. This 4 percent increase includes targeted increases, such as those for HIV/AIDS-related research, breast cancer research, minority health initiatives, prevention research, environmental cancer research, and gene therapy.

Continuing the Commitment to Health Security: The President remains committed to reforms that will guarantee insurance coverage to every American and contain costs for individuals, businesses, and Government.

The President believes Congress can and should address the unfairness in the insurance market; make coverage affordable for and available to children; help workers who lose their jobs keep their health insurance; level the playing field for the self-employed by giving them the kind of tax treatment other businesses enjoy; and help the families provide long-term care for a sick parent or a disabled child. We are committed to working with Congress to achieve these objectives and put America on the road to health security.

At the same time, we are proposing major increases for high-priority programs:

Ryan White Act -- HIV/AIDS Funding: The budget proposes $723 million for the Ryan White program, which provides HIV/AIDS treatment services. Since this Administration took office, funding for the Ryan White program has increased by 82 percent. Our proposal for 1996 will more than double Ryan White funding since 1993.

Immunizations: We propose $844 million for immunizations in 1996 to support the purchase of more vaccine to distribute through public health clinics and continued improvements in infrastructure to enable the Childhood Immunization program to meet its goal of immunizing 90 percent of the Nation's children by the year 2000.

Special Supplemental Feeding Program for Women, Infants, and Children: The budget proposes $3.8 billion for WIC, which will raise the annual average WIC participation levels to 7.4 million individuals, up from 5.9 million in 1993.

Long-Run Budget Outlook

This budget preserves and builds upon the deficit reductions that the Administration accomplished in its first two years. We expect the deficit to drop again in 1995, this time to $193 billion. After that, it will fluctuate in a narrow range -- rising to $197 billion in 1996 and to $213 billion in 1997 (due to several anomalies in the budget numbers), then falling to $194 in 2000.

More importantly, the deficit continues to decline in relation to GDP. It drops from 2.7 percent of GDP in 1996 to 2.1 percent in 2000. By this measure, the deficit reaches its lowest level since 1979.

Current law requires that the President submit budget estimates through 2000. By enacting the policy proposals in the budget, however, we can preserve the improvement in the deficit for at least the next 10 years. Looking beyond the year 2000, we anticipate rough stability in the dollar amount of the deficit through 2005. As a share of GDP, however, the deficit likely will continue its gradual decline, falling below two percent early in the next decade.

The major upward pressure on the deficit continues to come from health care. Although the reforms enacted in the President's economic program and administrative efforts to control costs have helped, the projected growth of Medicare and Medicaid spending remains very high. We project that Medicare will grow at an average annual rate of 9.1 percent over the next five years, and that Medicaid will grow at 9.3 percent.

This rapid growth comes in part from the corresponding rapid growth in the elderly population. Medicare benefits go primarily to the elderly, and almost 70 percent of Medicaid spending benefits the indigent elderly, blind, and disabled. Thus, the growth rates of these programs are not surprising. However, at those rates, Medicare and Medicaid spending will double every eight years, and will rise from 3.4 percent of GDP in the year just ended to 4.2 percent by 2000 and 4.9 percent by 2005. The growth in all Federal health programs, of which Medicare and Medicaid are by far the largest, accounts for almost 40 percent of the total increase in Federal outlays between now and the year 2000.

We expect the number of people participating in Medicare and Medicaid to increase, bringing insurance protection to some of our most vulnerable citizens. The Medicaid population will grow at a projected average annual rate of 3.8 percent between now and 2000.

But this expansion in covered populations explains a relatively small part of the increased Federal spending for Medicare and Medicaid -- and could be accommodated without undue pressure on the deficit. More important, from a fiscal standpoint, is that Medicare and Medicaid expenditures per beneficiary keep rising faster than inflation -- indeed, faster than inflation plus the general increase in real per capita GDP. These increases in health care costs cannot be solved in isolation from reform of the broader health care system.

What would the deficit be if health care costs did not rise disproportionately? If Medicare and Medicaid expenditures rose to accommodate increases in the beneficiary population, but the per capita expenditures were limited to the general rate of inflation and increase in per capita output, the deficit would fall to zero by 2005.

Conclusion

This budget builds on the President's success to date in strengthening the economy, investing in the future, projecting American leadership around the world, and making Government work better.

It will reduce the deficit, increase investments in important domestic and military programs, cut taxes for middle-income Americans, and begin a serious, cross-Government examination to sort out Federal, State, and local responsibilities.

We look forward to working with you, Mr. Chairman, and this committee on these proposals.

Chairman ARCHER. Thank you, Dr. Rivlin. Your closing line is definitely agreed to mutually. It is a hard job, and we need to work together on it, because if we don't work together, we won't get it done.

Ms. RIVLIN. Right.

Chairman ARCHER. I would only say that I would hope that we could work together on a glide path to a zero deficit, not to a $200 or $300 billion deficit. That is what divides us right now, and if we are willing to get together and make the tough choices that do the tough job, I believe we can do it.

I am curious about how we get there, though. As I understand your budget, we would have $1 trillion of additional debt over the next 5 years compared to what we have today; is that not true?

Ms. RIVLIN. The deficits would add to the debt by that much, but we believe two things: One, we have gotten the deficits under control. Two, outyear deficits are declining as a percentage of the GDP. This latter point is the way one ought to look at deficits and the national debt.

A deficit has significance in relation to the size of the economy. We have brought the deficit down from about 5 percent of GDP in 1992 to its current level of about 2.7 percent. This budget keeps us on a glide path to decline, cutting the deficit as a percentage of GDP in half by 1998 and down to 2.1 percent by the end of the decade. But we don't think that is enough. We must mutually come back to the fastest growing large item in the Federal budget, health care costs. Reducing the rate of growth of those costs is the key to additional outyear deficit reduction.

Chairman ARCHER. Well, I understand your response because we have heard it from Secretary Rubin and we have heard it from Laura Tyson. They say we really don't need to worry about getting to a zero deficit, and that all we have to do is be concerned about the debt and the deficits relative to the GDP. I just don't think the American people buy that.

We will be adding, according to what you just said, $1 trillion to the national debt in the next 5 years, irrespective of what the relationship is between the deficit and the GDP, according to your projections. If we have roughly an average 7 percent interest rate, that is, $70 billion a year of additional annual debt service, that must be maintained and paid for in every year thereafter; and that is what the American people don't understand when you talk about debt going down relative to the GDP.

In addition, Secretary Rubin said, and I wonder if you agree with this, that we should look at the analogy of a family that is able to increase its earnings every year. He feels there is nothing wrong with increasing debt because earnings are increasing; and therefore, relative to the total earnings of the family, the debt is not increasing, and therefore, that is what we are doing here.

Now, if that is to be accepted as valid in the way we pursue our goals, it must be assumed that we are forever going to increase our earnings and that there will never be an adjustment. We used to think about that in Houston, Tex., until the mid-1980s. We thought Houston could never take a backward step economically, and yet we found out that is not the real world. Families do have ups and downs in their earnings. If all you do every time you earn more money is to increase your debt but not increase it relative to your earnings, and the downturn comes, you are left with that magnificent debt, and you don't have the ability to sustain it.

The country, as we know, through business cycles is the same way, and I would just hope that the administration, while asking us to submit a detailed plan to get to a balanced budget, would do the same thing itself so that we could work together and have this interrelationship.

Now, let me also say that relative to something that was mentioned earlier on in your testimony, that you had runaway deficits and that you have now got them under control. Basically, if I understand what you said—and I have heard the President say, this is the first effort, real effort made at deficit reduction since about 1990?

That probably cost President Bush his reelection because he stood up and said, we have got to reduce the deficits. Why is that ignored? Wasn't that about a $500 billion deficit reduction as it was scored at that time?

Ms. RIVLIN. I would not ignore it, Mr. Chairman. I think the 1990 agreement was a good one. President Bush was right to engage in it and it did help. He didn't get much credit for it largely because the recession reduced revenues, and the deficit, therefore, did not go down. But were it not for the 1990 agreement, the deficit would have been even higher. So I would not be one to ignore the 1990 agreement.

But in 1993 we had to go beyond that and effect additional deficit reduction. We are proposing additional deficit reduction in this budget. That is, as you rightly point out, not the end. We are not satisfied with the deficits as they appear in this budget, and we are not saying that we are satisfied. We are saying that while the situation is a lot better than it was 2 years ago, we have to make more progress. One of the keys to more progress, we believe, is health care reform.

Chairman ARCHER. Well, would you encourage the President to give a little credit to the previous administration for deficit reduction, then, and stop saying that he is the first President to really do anything about deficit reduction? It would be very, very helpful to see that balance coming out of the administration.

Ms. RIVLIN. No one in the administration wants to knock the 1990 agreement, certainly not my good friend and colleague Leon Panetta, who was very much a part of that agreement. It is true, however, Mr. Chairman, that the deficit has come down for 3 years in a row, and that is the first time that that has happened since Harry Truman was President. We are very proud of that.

Chairman ARCHER. Well, I think that is movement in the right direction, and the downward trend is the thing we should try to work together on, but as I understand your budget, it now begins to go up again. It came down for 3 years in a row; and now under your budget, I believe the deficit goes up again. Now, you are going to say, oh, but not relative to the GDP.

Ms. RIVLIN. It goes up slightly in dollar terms but stays under $200 billion. The deficit picture in dollar terms is essentially flat, and in relation to the economy, it comes down. I believe that is a very important measure of how threatening a deficit is. When we arrived in 1993, we were in very serious trouble. Deficit projections were headed up and the debt was growing faster than the economy. Now we have gotten the situation under control. That does not mean, however, that the outyear deficits are not still a problem. They are.

Chairman ARCHER. Well, I just wish that we could get a statement from one of the administration witnesses to say that we will work with you to get to a balanced budget within the next 7–10 years so that we don't keep adding debt service charges, which will become the largest single expenditure in the Federal budget at $70 billion more per year in debt service charges as contemplated in your budget. This is, I believe, a tolerable situation.

But I have taken up too much time, and I recognize the ranking minority member, Mr. Gibbons, to inquire.

Mr. GIBBONS. Thank you, Mr. Archer. I always want to call you Alice out there, but I will call you Dr. Rivlin.

Ms. RIVLIN. That is OK by me.

Mr. GIBBONS. I feel that I have known you for so long and have followed your distinguished career and have learned a lot from you and expect to still learn a lot from you.

The President has laid out his figures, and we wait with baited breath to see the Republican figures on all of this. I have my own agenda. I look back—I think the worst vote I ever cast was the Gulf of Tonkin resolution, and the second worst vote I have a hard time identifying, but it was allowing somehow the budget deficit to get loose in the early eighties. I will take my share of the responsibility for that. I would like to live down those two votes.

So I am as excited as I can get when I hear tax reduction and all the nice reductions that are in the Contract and the President's tax reductions. I am going to be a deficit hawk this year because, as I look at the situation, never have we been in such a good position to pursue deficit reduction as we are right now, at least not recently. We have full employment or near-full employment, we have heavy factory utilization, the highest factory utilization we have had in 15 years. If we can't make a serious, serious, serious stab at reducing the budget deficit, Dr. Rivlin, I don't know when we can ever do it.

So I salute you for what you have done and for your budget and for everything else, but I am going to be a budget hawk and try to get the deficit down.

Now, in your statement you have a small article called Superfund; and I helped get the Superfund legislation passed, and I made another mistake there that I would like to rectify, and that is the whole idea of retroactive polluter pay. I think when we enacted polluter pay we never paid enough attention to the retroactive feature that was included in it, and I am. As I recall, this year the taxes to fund Superfund run out and this Congress has to renew them; and I told this to the Administrator of EPA, and I want to tell you so it will get right back to the White House, I am not going to support any of those extensions of those taxes unless we work out this retroactive liability provision. I don't know whatever got into us to make people liable for things that they did that were legal at the time they did them, and we could retroactively change the law on them and impose in some cases some crushing liabilities upon them.

I helped the administration last year try to pass that tax proposal that you all had, and I think I have been all the soldier on that issue I can be. I am not going to support the extension of any Superfund taxes, or of the Superfund legislation itself, unless we work out a satisfactory solution to that retroactive liability imposition that I think Congress improvidently imposed upon Americans; and frankly, I think the administration of the EPA law has exceeded the parameters that Congress ever envisioned in that regard. I want to clean up the mess, but I think the retroactive provision is just fundamentally and basically unfair.

If you all want to lobby me on that subject, I am laying myself wide open here with you right now. You have a hell of a hard convincing job to do on me, but I don't like political surprises; I didn't want to pull any of them on you all down there. I want to work with you, but I have kind of laid out my specifications, and you can get a copy of the transcript of this when this is all over and tell them, this is where Sam stands, and you all better start working on him if you are going to get his support in extending these taxes.

Ms. RIVLIN. I hear you, Mr. Gibbons, and I think it is a longer conversation than we can have here.

Mr. GIBBONS. I understand that.

Ms. RIVLIN. But we want to have that discussion, and we believe the tax should be extended, but that the Superfund provisions should be reformed. We have some proposals and would be glad to talk further with you about them.

Mr. GIBBONS. Well, thank you.

Thank you very much, Mr. Chairman.

Chairman ARCHER. Mr. Crane.

Mr. CRANE. Thank you.

Dr. Rivlin, is it true that our national debt will get to $5 trillion by the end of this year or very early next year?

Ms. RIVLIN. The gross debt—I am sure you have the number in front of you—I don't, but yes.

Mr. CRANE. Then, under the proposal, you are suggesting by the year 2001 we will be at $6 trillion?

Ms. RIVLIN. Right.

Mr. CRANE. Do you anticipate, or does the administration anticipate, some target date out there when we would round that bend, and instead of adding to it, at least it wouldn't be growing, or ideally it would be getting reduced?

Ms. RIVLIN. The first thing to do is to not have the debt growing faster than the economy is growing, and that is the situation as we look forward. I think it is very important that we have the debt rising slowly and the economy growing fast.

To get to a situation where the debt is actually coming down would require a surplus in the Federal budget. That might be desirable. We are a long way from that now. I think we should move in that direction, but it is really the relationship between the debt and the economy that is important.

At the end of World War II, we had a huge debt. We didn't reduce the dollar amount of the debt, but we didn't increase it very much over the next 25 years. Since the economy grew very rapidly in the years following the war, the burden of the debt and the debt service came down over a long period.

Mr. CRANE. One of the concerns I have is that debt service cost on an annual basis. What is it right now?

Ms. RIVLIN. Debt service is about 17 percent of the Federal budget. It is a very large portion.

Mr. CRANE. So what does that translate into in dollars?

Ms. RIVLIN. About $230 billion.

Mr. CRANE. About $243 billion. Say our national debt is at $6 trillion by the end of the century and assuming the percentage remains the same, what roughly would the dollar figure be?

Ms. RIVLIN. For debt service at the end of the century? About $300 billion.

Mr. CRANE. About $300 billion. The reason I am concerned about these figures is, if we didn't have debt service, we would be running budget surpluses right now on an annual basis.

When I first came here in 1969, that was the last time we had a surplus, and we have been going progressively deeper into debt every year since that time, and I guarantee you there is no cause-and-effect relationship.

Ms. RIVLIN. That is correct, Mr. Crane. Indeed, if we did not have to pay debt service on the portion of the debt run up between 1980 and 1992, which is most of the debt, we would be in surplus right now.

Mr. CRANE. I have a quote I am going to read to you:

> If the government was borrowing less, even running a surplus, more resources would be available for private investment to increase future productivity. Elimination of the Federal budget deficit would make a crucial contribution to income growth.

Can you attribute the source to that quote?

Ms. RIVLIN. It sounds like something I could have said.

Mr. CRANE. It is. It is out of your book, "Reviving the American Dream," and I salute you on that intent.

Let me ask one final question, and that is, why didn't the President, in his budget proposals, touch upon welfare reform as a means of effecting some economies?

Ms. RIVLIN. For a very simple reason. We have a welfare reform proposal which we put out in the last Congress. We want to work with the Congress on welfare reform. However, we didn't think that putting a particular proposal in the budget was the best tactical way to do that, especially since we were engaged in an active welfare reform discussion with the Congress and the Nation's Governors when the budget was released. But we are in favor of welfare reform, and we want to work with the Congress not only on how to do it but on how to pay for it as well.

Mr. CRANE. Well, thank you very much, Dr. Rivlin. I am consoled. I was worried that maybe the President had discarded that one. Thank you.

Chairman ARCHER. Mr. Hancock.

Mr. HANCOCK. Thank you, Mr. Chairman.

Ms. Rivlin, I am a little concerned about the statements that have been reported in which you said the deficit is down to $200 billion; therefore, we have got it under control.

I am a small businessman. I recently went back home and looked at what was going on in my business. The people that are managing my business, if they had said, well, we are only going to go $200,000 more in debt this year, therefore we have got our indebtedness under control, I would be making some changes, I will guarantee you, because there is no way you can do that.

Now I would like to ask this question. If the President would say to you and to Leon Panetta, we are going to get a balanced budget between now and the year 2000, and we would forget about having it under control just because we are down at $200 billion, we would forget about the GDP and that relationship, can it be done? If we continue to hear from the administration that it can't be done, then we are guaranteed that it won't be done.

Ms. RIVLIN. Oh, I am not sure the last part of the statement is true, because the Congress certainly could balance the budget.

Mr. HANCOCK. In other words, what you are saying is, it is all going to be up to the Congress?

Ms. RIVLIN. No, I am saying it is up to us together.

Could the budget be balanced by 2002? Yes, but it would require very deep cuts in many programs that people care about, and that is why the administration has been saying that those who believe that the budget should be balanced by 2002 have a duty to go beyond merely saying that. They have a duty to put a proposal on the table that shows what it would take to do that. Those who want additional tax cuts, in order to fund those tax cuts and still balance the budget, would have to make even deeper cuts in existing programs.

We have proposed a budget that includes tax cuts and we have shown exactly how we would pay for those cuts. In addition we have shown how we would contribute to additional deficit reduction, and we stand ready to talk about other ways of reducing the deficit in the years to come.

Mr. HANCOCK. If the balanced budget amendment passes through the Senate and is ratified, hopefully within the next couple years, wouldn't that drastically change the budget proposal that the President has submitted? Let's say that we had passed that 2 years ago. Wouldn't that drastically change the budget proposal? Should we have to have the balanced budget amendment to do what is right or to get the administration to do what is right?

Ms. RIVLIN. I don't believe that we should have a balanced budget amendment because the way to reduce the deficit is to do what the Clinton administration and the past Congress did together, enact specific spending cuts or revenue increases that are needed to get the deficit down. We did it, and it worked. I think that together we can do more of that. I would not favor, and the President does not favor, writing balance into the Constitution.

Mr. HANCOCK. You are saying that it has worked in relation to gross domestic product. It has not worked on an actual basis because we are going to be increasing the national debt over the next 5 years by roughly $1 trillion.

Now, if you take the inflationary factor out of it on a real dollar basis, then you have got an even worse scenario of where we are in relation to the gross domestic product. I mean, we can do a lot of things with inflation, but ultimately it catches us up just like it has in every major civilization.

Ms. RIVLIN. But let me be clear about what I meant when I said it has worked. In any terms you want to pick, it has worked in the last 2 years. In 1992 the deficit was $290 billion. This year it will be under $200 billion. That is real progress.

Mr. HANCOCK. Well, OK. But I don't think merely because we are down to $200 billion we ought to say, well, we are in good shape.

Ms. RIVLIN. No, and I am not saying that.

Mr. HANCOCK. OK, fine. Thank you.

Chairman ARCHER. Mr. Ford.

Mr. FORD. Thank you, Mr. Chairman. Dr. Rivlin, let me also welcome you to the committee, and before I get into the questions, let me make a comment—I might not be recognized anymore on this committee—and say to the chairman that I am awfully sorry if for 1 minute he has any questions in his mind in reference to my respect for him as chairman of this committee and even my respect for him prior to taking over as chairman of the committee.

I have known the chairman for quite some time. I have great respect for his ability as a member of this committee, as a very able legislator in this Congress, and certainly have all due respect for him as the chairman of this committee; and if I have suggested or signaled in any way on this committee that I do not have full respect, Mr. Chairman, I apologize right away, but I do feel that I have a responsibility as a member of this committee and one who represents the ninth district in Tennessee that when there are issues up before this committee, we have every right to discuss those.

As we dealt with tax preferences yesterday—I mean, you chose one that was dealing with affirmative action and I chose one that was dealing with oil and gas—that if we wanted to offset a bill that you pass—and it wasn't personal at all, Mr. Chairman, and I don't want you to feel that way at all. I certainly did not suggest or imply that your feelings on any particular issue—I mean, that issue was not put before this committee by Harold Ford; it was put before this committee by the chairman of this committee.

But, Dr. Rivlin, let me now focus on your statement on this budget. I was looking at the historical budget summary, and if I look back at 1977, 1978, 1979, and 1980, we had over a 4-year period an average budget deficit of about $55 billion a year, give or take, one way or the other, a little bit; and from 1982 through 1986, the deficit jumped from $128 billion, $207 billion, $185 billion, and $212 billion, yielding an average of about $185 to $190 billion, which increased that public debt and brought that public debt so high over a 4-year period.

If you look at the next 4 years, although it reduced somewhat the cost of leveling off of the defense budget, some increases in taxes, we had the deficits running anywhere from about $149, $155, $152 and $221 billion, once again, an average of about $165 billion a year.

Now, the Republican Contract With America is calling for a $196 billion deficit over a 5-year period, $700 billion deficit—not deficit, but to pay for the tax program, tax cut of about $700 billion; and I haven't seen how they are going to pay for that, I guess, through spending cuts, and we don't know who is going to be harmed by that. But the chairman was raising a question on the GDP.

Let me ask the question to you and maybe you can respond. Could you explain in laymen's terms why reducing the deficit as a share of the GDP is a significant accomplishment?

Ms. RIVLIN. Yes. Because the impact of the deficit on the economy depends on the size of the economy.

If you were comparing two countries and all you knew about them was the dollar amount of their deficit or their debt, you wouldn't really know anything. You would need to know, for instance, what two countries you are comparing. Are we talking about Belgium, or are we talking about the United States? Also, you would need to look at the impact of the deficit or the debt in relation to the size of the economy. If a business owed a debt of $100,000, it would make a difference whether that business was the corner grocery store or General Motors. Any given deficit or debt has to be viewed in relation to the size of the company, its revenues, its debt service, and so forth.

In the last 2 years, we have brought the deficit down in dollar terms. As we look ahead, it will become less of a problem because the economy will be growing and the deficit will not. I am not saying that the deficit isn't a problem, but it is less of a problem than it was 2 years ago.

Mr. FORD. But you find ways to pick up your tax cuts through spending cuts, and you offset it, you sort of pay for it some way, but do you think the American people really want these tax cuts when we are wrestling with the fact that we need to reduce the deficits?

I voted to support the constitutional amendment, which is, I guess, the opposite position of this administration, which I support strongly. I do think that we ought to have a balanced budget, but I don't think the Republicans with the Contract With America have the answer before this committee and this Congress to do that. I don't like the fact that we have to continue to have right at $200 billion deficits per year. I think we ought to take a closer look and not let this committee just think that we know what the American people want. If we are all sincere about it, we don't have to wait until the year 2002. We could find ways now.

The Clinton administration did it in 1993; you reduced those huge deficits that the Bush administration left on the American people, and we have it under control, and I think we ought to go one step beyond that, and we ought to find ways—not to give these tax cuts to satisfy, to please certain people in this country who make large contributions to political campaigns and win through the airwaves of this country the support that they might need. I think we ought to get serious about it and we ought to balance this budget.

Mr. HOUGHTON [presiding]. Thank you very much.

Mr. Zimmer will inquire.

Mr. ZIMMER. Thank you, Mr. Chairman. Ms. Rivlin, I read with interest Saturday's Washington Post, which indicated that you were a lonely advocate of more fiscal responsibility and a deficit that would decline in absolute dollars rather than only as a percentage of GDP in discussions within the White House. According to the Post, and I don't believe everything that is printed in the Washington Post, but according to the Post it wasn't until a meeting 1 week before the December 15 speech by the President on his Middle-Class Bill of Rights that the question of deficit reduction even came up for serious discussion.

I commend you for your apparent willingness to go it alone to try to convince the President and your colleagues in the administration that it is not good enough simply to reduce the deficit in terms of a percentage of the GDP. Your defense of that proposition today raises a question in my mind as to whether you really believe that this is good enough or whether you think it is preferable for the President to redeem his campaign pledge at least, and that was to reduce by 50 percent the deficit which, according to this article, you said would not be achieved with this policy.

Ms. RIVLIN. Well, we are all proud of our record on deficit reduction, and if you think about what the deficit would have been by now or by 1997 or 1998, it is clear that we are very close to having cut it in half. This is certainly the case if you look at the projections of what the deficit would have been without the deficit reduction plan of 1993.

At that time, the projection was that the deficit would be $387.7 or $388 billion by 1998. Given the track we are on, we will have cut that figure in half—1 year late if the campaign promise was supposed to have meant 1997—but that is still pretty good. We have also cut the deficit in half by 1998 as a percentage of GDP.

However, the President is not saying that he is satisfied with these outyear deficits. What he is saying is here is our plan for making a further contribution to deficit reduction, but we recognize that more is necessary, particularly in the area of cutting health care costs. We want to work with the Congress on that.

Mr. ZIMMER. Well, I admire your courage in arguing behind closed doors for more fiscal responsibility, and I admire your loyalty to the President in touting the company line, so I won't pursue this line of questioning any further.

But I will pick up on the comment that you made in passing that in order to get the deficit to zero, we have got to deal with the question of health care costs. The President's program submitted to Congress to reform health care in this country actually increased the deficit according to the CBO.

Ms. RIVLIN. It did not increase the deficit in the long run.

Mr. ZIMMER. But do you believe—and now the President is talking basically about insurance reform. What do you have in mind as a way to get a handle on health care costs that will actually get our deficit down to zero?

Ms. RIVLIN. That is a conversation we want to have with the Congress. I am not sure you can get the deficit to zero by focusing on health care alone, but you can certainly make a major contribution toward deficit reduction. We did not put proposals in this budget for controlling the costs of Medicare and Medicaid because we don't believe in cutting those programs as a way to pay for tax cuts. We didn't want proposed cuts for those programs to be picked up and used to pay for tax cuts for the rich. But we do believe that we have to talk about serious health care reform that will reduce the growth of health care costs for everyone.

Mr. ZIMMER. Thank you.

Mr. HOUGHTON. Thank you.

Mr. Coyne.

Mr. COYNE. Thank you, Mr. Chairman.

Dr. Rivlin, one of the big issues that is on the agenda here in Washington is welfare reform and certainly a part of the Contract With America; and I think the belief is that if you do reform welfare, you are going to produce great savings in the Federal budget. We have been told by some witnesses who have come here, who have had experience in welfare reform in their States, Governors and others, that if you really want to do welfare reform properly, you have to make an investment, and that it is quite possible that the investment in training and retraining, job placement, and day care may indeed be more expensive than the system we have today.

Could you comment on that?

Ms. RIVLIN. Yes. I think there is a common agenda in welfare reform upon which everyone is in agreement. We want welfare to be a temporary way station for people who are having difficulty making ends meet. We also want to provide training, child care, and other services to ensure that people who would otherwise be on welfare move to self-sufficiency quickly. You are absolutely right. That requires an upfront investment. All of the serious State and Federal welfare reform proposals recognize that.

Other programs can be cut to offset the costs of training, job placement, and child care. Although we may save money in the long run, initially reforming welfare to get people off the welfare rolls and into real jobs requires an investment.

Mr. COYNE. Thank you.

Mr. HOUGHTON. Thank you very much.

Mr. Johnson.

Mr. JOHNSON. Thank you, Mr. Chairman.

Dr. Rivlin, I am reminded of flying airplanes because that is what I did for about 29 years, and still do some, and I am sure you have; and when you talk about glide path to success on the budget, you know you can put an airplane on a glide path, and if you don't correct the glide path enough to make a smooth landing, you are going to crash, and I think that is what you have got us aimed at is a path to total destruction.

I wonder what you would tell a pilot if you said, hey, with reference to the sky we have changed your glide path, but with reference to the ground it hasn't changed at all and you are going to crash. Now, what would you tell the average American citizen if he said, I just can't support my debt any longer? I know what you would tell him, you would tell him to declare bankruptcy, chapter 11 or whatever.

Can I ask you, what would happen if everyone called their notes on the U.S. Government?

Ms. RIVLIN. Well, that is not about to happen.

Mr. JOHNSON. I am what-iffing you.

Ms. RIVLIN. Some people would gain and some people would lose.

Mr. JOHNSON. What would happen to the U.S. Government?

Ms. RIVLIN. Most of these notes are held by other Americans.

Mr. JOHNSON. Aren't there some 13 or 14 percent of them held by foreign countries?

Ms. RIVLIN. Yes, but that is a fairly trivial amount.

Mr. JOHNSON. What is trivial about 14 percent of our debt?

Ms. RIVLIN. I think if you are worried that foreigners will have so little confidence in the U.S. Government that they will refuse to hold U.S. Government securities, you are worrying about something that at the moment is——

Mr. JOHNSON. I am what-iffing you. What happens if someone does call our notes?

Ms. RIVLIN. I don't think this is a serious problem.

Mr. JOHNSON. I am aiming at the deficit. You keep saying it is OK to have an increasing deficit.

Ms. RIVLIN. No, I didn't say that at all. I said that the significance of the deficit has to be viewed in relation to the economy. We have brought the deficit down a lot, but we are not satisfied. We need to do more.

Mr. JOHNSON. Wouldn't you agree with me that you cannot start to get at the debt until you get the deficit to zero?

Ms. RIVLIN. That is right, and I think that the economy of the United States can support the current level of debt and even an increasing level of debt. But that is not to say that an increasing debt is desirable.

We all ought to be looking at what kind of economy we want to have a few years from now. What kind of standard of living do we want for Americans? Now, getting the deficit down will help the future standard of living. Reducing the deficit will also help us to invest in people and enhance our competitiveness in a world economy, and that is what really matters; there is a tradeoff between how much you want to do that and how much you want to reduce the deficit.

Mr. JOHNSON. I think we should try to get at the debt.

Can you tell me—I know in the article that Mr. Zimmer was talking about you were arguing, I believe, against tax reduction and for more deficit reduction, which is kind of appealing. However, the President apparently chose the course of some tax reduction, and can I ask you, what is the difference between a child under 13 and one over 13, and why is it important to have a tax credit for children under 13 but not over 13?

Ms. RIVLIN. We felt that those were the years when families were bringing up young children. We are talking here about working families. This credit phases out between $60,000 and $75,000, so we are not talking about upper income families. We are talking about average people—those were the years that——

Mr. JOHNSON. A guy who makes $80,000 is not average?

Ms. RIVLIN. No, statistically he is not very average.

Mr. JOHNSON. He is not an average American?

Ms. RIVLIN. He is quite high.

Mr. JOHNSON. Anybody who makes over $65,000 a year is not an average American citizen?

Ms. RIVLIN. The people who make $80,000 a year are more privileged than most people. They may not think so, but statistically they are.

But you asked what the difference is between a 12-year-old and a 13-year-old. Not very much, but you have to draw the line somewhere, and our view was that this tax cut should be concentrated on working families with kids who are having a hard time making ends meet.

Mr. JOHNSON. I would suggest that it probably costs more for teenagers than it does under age 13.

I thank you, Mr. Chairman. My time has expired.

Mr. HOUGHTON. Thanks very much.

Mr. Collins will inquire.

Mr. COLLINS. Thank you, Mr. Chairman.

Ms. Rivlin, I have a great deal of concern about comparing the debt against the gross domestic product. I have concern about the analysis you used of $100,000 debt, whether it is the grocery store or GM. My concern is the comparison of government "investment" or spending money to how a business invests money. If a business invests money unwisely or nonproductively, then they won't get a return to be able to retire that debt. When you go back and you look at the debt that the government has incurred since World War II and the fact that we were able to retire that debt after a certain period of time, I think you will find a great deal of difference in how the government paid off those debts versus how the government operates today.

Is that not a fair statement?

Ms. RIVLIN. How the government was investing funds?

Mr. COLLINS. Yes.

Ms. RIVLIN. Well, government programs have changed over the years, but this administration has emphasized shifting money from less productive to more productive types of expenditures. By this we mean things that will give people more skills in the future, improve science and technology, and improve our infrastructure. We have emphasized those kinds of public expenditures. That does not mean private investments aren't important. That is another reason for reducing the deficit, but what the government does makes a difference. We can help improve the skills of the work force. That is very important to the future of America.

Mr. COLLINS. But we have created so many types of programs, something like 154 different types of work training programs. We have an abundance of things that we have splintered off through government "investments" or expenditures that are not productive. They are not working, and that is one of the reasons why we are considering block grants.

Ms. RIVLIN. You will see that in our budget. It is a common theme.

Mr. COLLINS. You used the word "partnership" versus "block granting." I have been a small businessman, as have several other of our colleagues, for a number of years, and I have had partnerships. I have never had one that succeeded for a long period of time, and it worries me to use that word. I have heard some of my-side-of-the-aisle colleagues use the word "partnership," too.

When we look back at the State governments and the local governments, they are an entirely different entity; they are self-incorporated. When we say we are going to be part of a partnership, we are going to have strings attached, mandates to go along with that partnership. Strings mean we are going to control how they use those funds and, really, funds that we get from the people of those jurisdictions.

The "partnership" word bothers me. That is the reason I like the block grants without so many strings attached or so many mandates and more and more flexibility.

You agreed, too, with Mr. Hancock that we could balance the budget by the year 2000, but to do so would probably threaten a lot of programs that people like. It has been mentioned earlier, too, that a lot of those programs improve people's lives, but is it not true that a lot of those programs, too, make it very difficult on other people's lives? I am referring to the Robin Hood style of government we have where we take from some and give to others.

Ms. RIVLIN. Well, I think lots of people differ on what is an important government program. The programs this administration has emphasized have broad support. For instance, everyone benefits when, in a program like Head Start, we help children get a better start in life and do better in school. That kind of program doesn't hurt anybody.

Mr. COLLINS. My point is, in order to help that family with the Head Start need, you are going to have to take from another family who probably has a need, too, and this will lessen their ability to provide for themselves. That is the Robin Hood style of government that I am speaking of. I think we have created too much of the Robin Hood style, although all of us have compassion and want to help those who are in need, but we have got to go back and redefine what is really need.

Thank you.

Ms. RIVLIN. I think we can agree that not all government programs are as effective as they should be. However, I think what you see in this budget is an attempt to look at what is working, what is not working, and make programs that are not working more effective.

Mr. HOUGHTON. Thank you very much.

Mr. Rangel will inquire.

Mr. RANGEL. Thank you, Mr. Chairman.

Let me thank you, Doctor, once again for being before this committee. I know it sounds like a broken record, but I am going to talk about drug control, and I see that there has been an increase of $1.3 billion in drug control, and that brings it up to $14.6 billion.

The thing that has bothered me over the years is that everyone says, you are right, but no one says what has been done. When Dick Darman was in charge of your office, it took me years to get him to find out what the Nation was losing in the war against drugs. I am going to ask your office, would you be kind enough to take the costs—and I am willing to give you the papers that he shared with us, because at that time he said when you included lost productivity and lost revenues, we lost every year $350 billion. Of course, that was years ago. Now we see that there is a concentration on treatment, but when I ask questions about treatment it seems that we have the block grants, so none of the Federal officials can say that they know what is going on in treatment.

Having been in the State legislature, I know that the Governors normally rely on the members of the assembly and the Senate to determine the quality of treatment, but in all of the treatment centers I have seen that are good, the addicts tell me they are good because they always go there, and they use them all, and there never seems to be any job training or job at the end of the treatment, and they go into these programs illiterate and they come out drug free and illiterate; and after they are on the streets and there are no jobs and they are depressed, the only friends they sometimes have are those that are in the drug area. So I have always fought for more money for treatment and treatment on demand and all of these things, but nobody ever in any administration has been able to tell me, what kind of treatment are we talking about? Could you?

Ms. RIVLIN. Well, we have put more money into drug treatment programs. We would be happy to talk about exactly what this money goes for, what constitutes effective treatment, and how to fund those programs that are most effective. But you are quite right. Effective treatment programs must be part of a package that includes job creation. I think this budget's emphasis on job creation, training, and making the whole system work better for workers—including ex-addicts—is an important step in that direction.

Mr. RANGEL. Well, Doctor, like I said, the frustration is, everyone says I am right, but I don't think that you have that much control over these block grants.

I mean, we are giving the States flexibility. Everyone wants flexibility. People closer to the problem have the answers, and they don't have the money really to do the job that would be necessary if they have got to educate these people and make them prepared for work. But one thing you could do is you could really provide for this committee the statistical data as relates to the impact on drug addiction, the cost of crime, the cost of the health, and the cost of—economists are always able to measure, I don't know how, the lost productivity as we have with these people, 1 million people in jail, where 70 percent of them could be working, and they are in jail, a number of people in the hospital with drug-related diseases that should be working, that would be very important.

Can your office do that?

Ms. RIVLIN. Yes, we will work with Lee Brown and give you what estimates are possible. Obviously, there is no firm number. But we all know that the costs of drug-related problems are very large and have serious implications for our country.

Mr. RANGEL. But economists have this strange way of doing it all the time, so I don't see what Lee Brown would have to do with it. It would seem to me that you would go to HHS and ask how many of the cases in this hospital are drug related, and then you would go to the criminal justice system and you would ask the Attorney General, because Lee Brown is depending on all these other people.

Ms. RIVLIN. That is absolutely right. I suggested that he and I work together on this because it is a drug-related matter, and that is his job.

[The following was subsequently received:]

COST OF ILLICIT DRUG USE

Government Spending for Drug Control is Substantial

Federal, State, and local governments spend roughly $25 billion on drug control efforts, or $0.50 for every dollar spent by drug consumers in the illicit drug trade. Approximately 63 percent of the Federal drug control budget is directed to law enforcement programs, with the balance directed to treatment and prevention programs. Most State and local government spending is directed to the criminal justice system (79 percent), with the balance going for education and rehabilitation (21 percent).

Total federal spending in FY 1994 was $12.1 billion. The request for FY 1996 is $14.6 billion. A breakdown is found in both the 1995 National Drug Control Strategy and the separate Budget Summary.

The figures for State and local spending come from an Office of National Drug Control Policy (ONDCP) report released in December 1993, titled *State and Local Spending on Drug Control Activities: Report from the National Survey of State and Local Governments.* According to that report, State governments spent $7.45 billion on drug control in 1991. Local governments spent $8.46 billion.

Another Cost Category Relates to the Economic Costs of Money Spent for Illegal Drugs

The illicit drug trade is a drain on the U.S. economy. An ONDCP study titled "What American Users Spend on Illicit Drugs" shows the retail value of the illicit drug business in 1993 totaled $48.7 billion. The bulk of this money goes for cocaine ($30.8 billion). Marijuana and heroin make up the rest. In addition to resources wasted on drugs, drug use leads to many other costs -- welfare for the children of drug users, health care costs, and the costs of crimes related to both drug trafficking and drug use.

Social Cost of Drug Use

A Brandeis University study endorsed by the ONDCP estimates the total cost of drug use at $67 billion annually. Almost 70 percent of this amount is attributable to the costs of crime; the remainder reflects medical and death-related costs. In particular, $3.2 billion (4.8%) was for medical expenses, $8 billion (11.9%) related to the costs of illness, $3.4 billion (5.1%) was related to deaths, and $46 billion (68.8%) fell into the "other related" category (costs of crime, incarceration, and loss of productivity).

Mr. RANGEL. Thank you.

Mr. HOUGHTON. Thank you.

Mr. Ensign.

Mr. ENSIGN. Thank you, Mr. Chairman. I want to take up a couple of the points that have been made earlier and relate it back to business, because I do agree somewhat with the arguments about the deficit as it relates to GDP and that it is better to have it as a lower percentage of GDP than it is. Obviously, the other way around, the way it was back in 1992 is a proper direction to move toward. If you look at businesses, and the analogy has been made that if you look at a business that takes on a certain percentage of debt, as long as that percentage of debt can be serviced, the relative health of the company is good.

But also knowing the public markets and knowing how some companies, how well their stock does, one of the factors that Wall Street looks at is the percentage of debt that they do have on that company; and certainly the lower the percentage, which is the direction that we are going, the better. That means that in general a company's fiscal house is in order.

I think what we saw a lot in the eighties was companies taking on more and more and more debt, but they were growing and so it looked OK; but when it comes down—and that is the fear that we share now. As we are growing it may be looking pretty good, but I think what we need to do is, we need to make the tougher cuts. We have got to not only get to a balanced budget, but we have got to get to surplus budgets so we can start working on the debt, eventually pay off the debt, have a rainy day fund so when you are in trouble in a country, when you have a healthy economy, you can prepare for those times.

Your comments?

Ms. RIVLIN. I think I am on record in a past life of having said that a surplus, on the average, over the business cycle would probably be a good thing for a country such as ours, which has a low private savings rate. To say that you are running a surplus in the Federal budget means that the Federal Government is reducing its debt. Thus, the government is doing its part of saving and redeeming the debt so that there will be more funds available for private investment. As a long-run goal, that is certainly a worthy one. It should happen, but it makes a difference how you get there.

Mr. ENSIGN. How long should that long-run goal be? Are we talking 20, 30, 40 years?

Ms. RIVLIN. I think it is hard to say.

Mr. ENSIGN. The problem I have with that "hard to say"—and Secretary Rubin was here the other day, and the old saying about, "If you don't aim at the target, you are sure not to hit it"; all of us learn the basics: You need to set goals and target dates, and things should be time certain. One of the first things you learn on goal setting is, everything should be date and time certain, and if you don't, you will never get to that, and that is what we are saying and why we have set 2002 as our goal date to get to a balanced budget, so that we can work toward those tough choices that we need to make to get to that balanced budget.

Ms. RIVLIN. Well, the problem is that countries have multiple goals, and it doesn't make sense to sacrifice some important goals for others. The whole——

Mr. ENSIGN. You have to make that choice. You have to make tough choices, even a country.

Ms. RIVLIN. Can I finish the sentence?

Mr. ENSIGN. Yes.

Ms. RIVLIN. You have to make tough choices, but it would not make sense to aim so single-mindedly at balancing the budget that you forgot why you were trying to achieve balance. You attempt to achieve balance in order to get a better economy. But if the way you get to balance is by cutting productive government investments or throwing the economy into recession by moving the deficit down too rapidly, it is self-defeating.

Mr. ENSIGN. I think the other thing we have to keep in mind, one of the reasons that we are doing it is so we don't put this burden on our children and our grandchildren; and that is something that we lose focus on sometimes. We have this debt that has been put on us and if we do not act responsibly, we are just putting it on to future generations to make those tough choices.

Thank you, Mr. Chairman.

Ms. RIVLIN. Reducing the debt is one thing we can do for our children. But we can also make sure our children have good schools, get a good education, and also have an economy that will support higher wages for them.

Mr. HOUGHTON. Thank you very much.

Mr. Christensen will inquire.

Mr. CHRISTENSEN. On that note, it is not the role of the Federal Government to be involved in local school systems. It is the role of the local citizenry and the States; not the role of the Federal Government. There is where we have a real difference.

It is not the role of the Federal Government to set a minimum wage, and that is why we have a big disagreement with the administration. The markets will dictate what the wage should be.

Right now, for example, in Omaha, Nebr., where I am from, the market's prevailing wage is far above the minimum wage, so I guess we would have a real disagreement with that. Earlier, talking to Mr. Johnson, you took a swipe and said "tax cuts for the rich." Mrs. Rivlin, I know you didn't mean to say that. You weren't calling our senior citizens rich, were you?

Ms. RIVLIN. I was referring to the fact that the tax cuts proposed in the Contract With America are much more oriented toward aiding upper income people than those of the Clinton administration.

Mr. CHRISTENSEN. So you were calling our senior citizens rich?

Ms. RIVLIN. I don't remember that we were talking about senior citizens. We were talking about two different kinds of tax cuts.

Mr. CHRISTENSEN. No, you said "tax cuts for the rich," and I just want to make sure we get you on record that you weren't calling all senior citizens rich.

Ms. RIVLIN. Some senior citizens are rich and many are not.

Mr. CHRISTENSEN. Those making above $11,280 would you call rich?

Ms. RIVLIN. Some senior citizens making above that amount are rich and some are not.

Mr. CHRISTENSEN. I am sure you weren't calling our working moms and dads with children rich, were you?

Ms. RIVLIN. I don't know what this line of questioning is for. Rich people are people with high incomes.

Mr. CHRISTENSEN. It was the swipe that you took that I didn't appreciate because of all the various provisions that we have looked at. For example, 60 percent of our capital gains tax cut is going to go to those people that make $75,000 or less. The tax cut that we talked about yesterday and passed in this committee, I am sure you weren't calling self-employed small businessowners rich, because the 25-percent health care deduction is going to go to 3 million of them.

I appreciate the ranking minority member's comment earlier today about how it is going to be everybody's responsibility and the fact that it wasn't just President Reagan or President Bush, but it was the entire Congress that needs to take responsibility for what happened to the debt.

I want to find out what happened behind closed doors when you and the President and the other people on his task force were making decisions on not to seek a balanced budget. What was said? Was there ever anything said that, well, let's let the majority put their bill out there; let's let them do the heavy lifting and make the major cuts so that they take the hit. Was there any comment made to that area?

Ms. RIVLIN. I am not going to discuss internal discussions that took place in the White House. The President likes to listen to all the different views. The difficult questions that were being discussed were——

Mr. CHRISTENSEN. Mrs. Rivlin, I am not asking for you to divulge any secrets. I just want to know, was there any discussion brought up to the fact that let's try to balance the budget by the year 2002——

Ms. RIVLIN. I said I am not going to talk about internal White House discussions. The important thing for us to be focusing on today is the tradeoff between reducing the deficit faster and sharing the benefits of recovery with average families. We believe that our budget is a compromise on that tradeoff. It reduces the deficit further and emphasizes the need for sharing the benefits of recovery with average families, both now and in the future.

Mr. CHRISTENSEN. I appreciate some of the things that you have stood for in the past and the fact that you have been on the cutting edge of trying to get the administration to go further, but I have to tell you that $200 billion a year deficits, adding $1 trillion to our debt, is not an example of being a deficit hawk. I would encourage you to continue to prod the administration toward a balanced budget.

We have our own problems to get a balanced budget amendment. We need your help in this area because the American people want to see their government live on a balanced budget, and I truly believe that you want to see that, too, and maybe your hands are tied. I would like to know what is going on, though, behind closed doors and who they are setting up to take the fall.

Ms. RIVLIN. Well, we would like to see how those who favor both getting to balance by the year 2002 and offering much larger tax cuts are going to pay for it.

Mr. HOUGHTON. Thank you very much.

Mr. Levin.

Mr. LEVIN. Hello, Dr. Rivlin. You were kind of pushed on some of your statements. Just so the record is clear, Mr. Christensen, I think Dr. Rivlin was referring to a Treasury study of all the tax proposals in the Contract, and I would like to just read to you the Treasury analysis, Mr. Christensen.

Mr. CHRISTENSEN. What is that?

Mr. LEVIN. I will just put them in the record. I just wanted to read to you the Treasury analysis of the Contract proposals because you implied that Dr. Rivlin's facts were wrong: 27.3 percent would go to families with income over $200,000 and more, 24.8 percent to families $100,000 to $200,000, and 23.7 percent to families $75,000 to $100,000; so that means 52 percent would go to people $100,000 or more, and if you add those $75,000 and more, that is the upper quintile, that would be about 70 percent.

Mr. CHRISTENSEN. Would the gentleman yield?

Mr. LEVIN. Sure.

Mr. CHRISTENSEN. My comment was that for the last 3 weeks we have heard a lot of class warfare talk and we have heard about tax cuts for the so-called wealthy. Being a new member on this committee, I just wanted to make sure that some of the areas that I outlined here were not her description of tax cuts for the rich.

Mr. LEVIN. But two things: To point out an income distribution isn't class warfare. Is income distribution irrelevant?

Mr. CHRISTENSEN. For the last several months we have heard nothing but demagoguery on the part of a few members about how it is terrible and it is rotten and it is evil for people to be successful in life and to create jobs and to earn a better living, and I guess it just gets a little tiring on our side to hear that.

Mr. LEVIN. That isn't my position. I don't think it is the position——

Ms. RIVLIN. It is certainly not my position.

Mr. LEVIN. I will ask Dr. Rivlin her attitude about growth, but I don't think it is irrelevant to look at a distribution table.

Mr. PORTMAN. Will the gentleman yield for a moment?

Mr. LEVIN. Yes.

Mr. PORTMAN. I believe what Mr. Christensen was referring to—and I believe the record will support this—in response to a question from Mr. Johnson, I think Dr. Rivlin said that the administration didn't want to use Medicare savings to support tax cuts for the rich. I guess my only comment to that would be that the administration made a much broader decision, which was not to support it for deficit reduction generally, much less for tax cuts for anybody. I think that was the context—I believe.

Mr. LEVIN. No, but what Dr. Rivlin—I will give her a chance to speak herself—is saying is that they don't want Medicare cuts going for tax proposals that primarily benefit upper income families.

Mr. PORTMAN. If the gentleman would yield. Of course you are describing the administration's tax proposals in that way because that would have been the offset in its budget, of course.

Mr. LEVIN. But it isn't. I mean, Dr. Rivlin, there is a tax cut proposal in the President's proposal, right, aimed at middle-income families?

Ms. RIVLIN. Yes.

Mr. LEVIN. Is it paid for by Medicare savings?

Ms. RIVLIN. No, it isn't.

I was really making two simple points. One is that our tax cut is much more limited than the tax cut proposed in the Contract With America. The administration's tax cut focuses more on average families and on encouraging education and training; we did not put Medicare cuts in our budget, and we did not pay for our tax cut by Medicare cuts. We don't think that is a good thing to do.

Mr. LEVIN. Let me just ask you, it will take you more than 30 seconds, but the deficit does stay—I am going to ask you, I think, a somewhat tough question—at kind of a stationary level; not in terms of GDP, it goes down. Give us a 1-minute or a 30-second answer, if the chair will indulge, in why it is worthwhile to take the $60 to $70 billion in tax cuts and apply them to tax cuts for middle-income families instead of reducing the deficit over 5 years.

Ms. RIVLIN. Well, one of our goals is raising living standards for average people. Now, bringing the deficit down helps to do that because it fosters investment generally, but there are other ways of raising living standards. Our proposals to change the Tax Code to give some immediate relief to working families with young children and to foster investment in the education and training of people so they have better jobs and higher wages in the future provides another means for raising living standards. We believe that our tax deduction for education and many of the spending programs that are in the budget, especially the GI bill for American workers, would all help to achieve our goal of improving living standards for average people.

Mr. LEVIN. Thank you.

Thank you for the indulgence of the Chair. Thank you.

Mr. HOUGHTON. Thank you.

Ms. Dunn will inquire.

Ms. DUNN. Thank you very much, Mr. Chairman, and Dr. Rivlin, welcome to this panel. I would like to take advantage of your background to ask you a couple of questions, the first one being very, very general; and the second one, far more specific to my part of the country, which is the Northwest.

I am as worried as everybody is about the size of the interest payment on our debt. During a campaign I ran a couple of years ago, I got questions from folks about why we couldn't add to the budget a payment on the principal of the national debt. Could you talk to me a bit about that, the pluses, the minuses, why, why not, the general thinking?

Ms. RIVLIN. Well, the debt is simply the sum total of government borrowings. As many people have pointed out here today, while the government still runs a deficit, it is still borrowing additional money which causes the debt to grow. The first step in reducing the debt, therefore, is to get the deficit to zero. If you establish a fund now to reduce the debt, while the government is still borrowing money, it would essentially be meaningless. The debt will grow as long as there is a deficit.

Now, as I pointed out, the seriousness of the debt problem depends on whether the economy is growing. If the economy is growing faster than the debt is growing, it is a much less serious problem.

Ms. DUNN. Thank you.

The second question, I am interested in your thinking on the Bonneville Power Administration mentioned in the budget. You suggest turning it over to a government corporation. There has been talk about privatizing the BPA. Those of us in the Northwest are very concerned about that talk because we believe that it results in false revenue estimates, something like $7 billion that we can't count on because we can't count on a buyer for the Bonneville Power Administration; and the President in his budget has said that it should be turned into a government corporation.

Could you give me the background on that?

Ms. RIVLIN. Yes. We are not proposing privatizing Bonneville for the reasons to which you allude. While Bonneville has heavy debt, we think it would run more efficiently as a government corporation. It is not a massive change and I think it would allow Bonneville to do some things more effectively. The change to a government corporation also would not increase rates for customers.

We are proposing gradual privatization of some other power marketing authorities, but not Bonneville.

Ms. DUNN. I had thought that it would increase the rates in a minor way, but not the way that privatization would; but the reason it would increase the rates is because we would be refinancing the long-term debt from the 3-plus percent that it was originally funded under to 6.7 percent, and also making a $100 million downpayment in order to—a premium that would allow us to go through that refinancing. Is that what——

Ms. RIVLIN. Well, if I may, I would like to give you a more detailed answer on Bonneville for the record or subsequent to the hearing.

Ms. DUNN. Thank you.

Thank you, Mr. Chairman.

[The following was subsequently received:]

May 25, 1995

Answer to Congresswoman Dunn's Question on Bonneville Power

In his fiscal 1996 budget, the President recommended that the Bonneville Power Administration (BPA) be changed into a wholly-owned Government corporation so that it can operate in a more business-like way.

Currently, BPA is subject to many Department of Energy, General Services Administration, Office of Personnel Management and other agency requirements that, BPA says, impedes its operational efficiency. BPA believes that, free from many of these requirements, it will have the autonomy and flexibility to operate more efficiently and at lower costs. BPA and the Energy Department estimate that this change could save $15 to $20 million annually.

The Administration's support for any government corporation proposal is dependent on its review of the draft BPA legislation. This review is now under way.

As I indicated in my testimony, this change should not involve any additional cost to BPA ratepayers. Indeed, the objective is to allow BPA to operate more efficiently so it can lower ratepayers' costs.

With respect to refinancing BPA's existing appropriation debt, the Administration proposed such legislation last year and endorsed it this year.

You mentioned that last year's "refinancing" legislation would have required BPA to pay $100 million above the net present value of BPA current appropriation debt repayment requirements. This was deemed the minimum equitable consideration due the Treasury in return for the Treasury's allowing BPA to "lock in" below-cost Treasury financing that BPA and its customers enjoy. This Treasury financing subsidy costs taxpayers more than $300 million every year. Most of it results from the difference between the extremely low interest rates that BPA used on its appropriation debt and the Treasury's much higher cost of borrowing at the time BPA borrowed the funds.

Mr. HOUGHTON. Thank you.

Mr. English.

Mr. ENGLISH. Thank you.

Dr. Rivlin, I want to briefly revisit something that I think Mr. Johnson touched on in his questioning and perhaps was not in a position to amplify on, and again I don't want to intrude into any administration council fires, but I would like to get an explanation from a public policy standpoint of why the administration chose to limit its child tax credit specifically to families with children under 13, because I have been puzzling through what the distinction is between providing this credit for younger children as opposed to teenagers, and I haven't been able to come up with a meaningful public policy way of distinguishing those families, No. 1.

No. 2, I believe that the costs are substantially larger for teenagers—I know that was my parents' expert finding with me—and so I wonder if you could give us what the rationale of the administration was, apart from revenue. I understand there is always a need to shape a proposal to resemble the revenue available, but apart from the revenue, is there a solid reason for targeting the tax credit this way?

Ms. RIVLIN. Well, it was really a way of targeting the tax credit at younger families who are just getting started. Teenagers are very expensive. Mrs. Clinton actually pointed that out, as she is the mother of a teenager. Nobody is saying that it is cheaper to have a 16-year-old than an 11-year-old. It is not. But the effort was to target young families struggling to get started. It was our feeling that a focus on young families with younger children at income levels that made it difficult to make ends meet was the most effective way to target the tax credit.

Mr. ENGLISH. OK. So ultimately this was at least partially revenue driven, given the fact that you had a certain amount of money, but this was a better way of targeting the available revenue; is that fair to say?

Ms. RIVLIN. That is right.

Mr. ENGLISH. OK.

On a second point, with regard to the design of your tuition and training tax deduction, did you look at the possibility of providing a limited targeted tax credit as an alternative, and would the administration be receptive to that kind of an approach?

Ms. RIVLIN. We talked about the possibility of doing a credit rather than a deduction and would be happy to talk about it further. The point is to get money to people who want to invest in themselves and their education.

Mr. ENGLISH. Another question I had had to do with testimony before our Social Security Subcommittee by Dr. Shirley Chater, the Commissioner, who argued that the Clinton administration would be receptive to the idea of raising the earnings limitation on Social Security, but only to what she described as a moderate amount, an increase of $1,000 per year for 5 years.

Now, raising the income threshold from $11,000 to about $17,000 seems to me to be a very modest proposal. Would the administration—given the fact that we can, I suspect, address the revenue side of the equation, be receptive to a more substantial raising of the threshold as the Contract proposes?

Ms. RIVLIN. We are very wary of raising the threshold too much because it costs a lot of revenue and it doesn't necessarily——

Mr. ENGLISH. In the short term, but in the long term there is a recapture.

Ms. RIVLIN. There is some recapture in the long term, but it certainly costs revenue in the near term. The notion of Social Security was that it was to be for people who are retired. The amount of money you are earning determines whether you are retired.

Mr. ENGLISH. So we have a philosophical disagreement on that probably?

Ms. RIVLIN. We may have.

Mr. ENGLISH. Thank you very much for your testimony.

Ms. RIVLIN. Thank you.

Mr. HOUGHTON. Thank you.

Mr. Payne.

Mr. PAYNE. Thank you very much, Mr. Chairman.

Dr. Rivlin, thank you very much. I suppose I may be the last or almost the last person who will question you today.

I first wanted to comment on what Ms. Dunn said earlier in her concern about Bonneville. My folks are concerned about SEPA, the Southeastern Power Administration, but rather than get into that here, I would rather work with the administration as we move forward to try to better understand that proposal and to make sure that it is one that is both fair and equitable for the taxpayers as well as the customers.

Ms. RIVLIN. As well as the ratepayers. We very much agree with that.

Mr. PAYNE. Thank you. I am one of the people who supported the balanced budget amendment. I am very interested in seeing us get on a glide path where we can, in fact, by the year 2002, find our way to no budget deficit.

I am concerned, though, in this committee, the discussions that we have had thus far this year have centered around the Contract With America, and both the Joint Tax Committee and the Treasury have suggested that if we implement all of the tax provisions that are being put forth, we will add to the deficit some $200 billion over 5 years or $700 billion over 10 years; and the budget that is being submitted by the administration, as I understand it, would have for the middle-income tax cut other savings provisions, some $63 billion in potential increase in the deficit.

Ms. RIVLIN. The tax cut will cost that much, right.

Mr. PAYNE. Now, that proposal versus the Contract With America, as I understand it, which would cost comparably $200 billion, means that the difference, or $137 billion, would have to be found in savings and various cuts over the 5-year period just for us to stay exactly where the administration's budget is now before we begin any kind of deficit reduction. Is that an accurate depiction?

Ms. RIVLIN. If the majority comes up with only enough offsets to pay for their tax cuts, then they will have a budget that does not reduce the deficit at all.

Mr. PAYNE. I think that there are many of us who see many of these items in the Contract With America as desirable, but are very concerned about the cost and are looking at the deficit reduction as being extremely important and something that we need to address ourselves to first.

Let me move very quickly, since I have a limited amount of time, to something that I am trying to understand better. In the President's budget, HCFA has looked at the baseline for our government health care programs. As I understand it, the Medicare baseline has been reduced from 11.9 to 9.9 percent growth rate, Medicaid has been reduced from 13.7 to 8.2 percent in terms of the growth rate; and yesterday Secretary Rubin said that what all this meant was that in terms of the 5-year budget that we had actually saved some $212 billion, or had potentially reduced the deficit by that amount as a result in the change of the baseline that had been set forth by HCFA.

I have several questions. No. 1, is this driven to some extent by the private sector reductions that we have learned about? No. 2, is it driven to some extent by the move to HMOs or policy driven? No. 3, might we expect further reductions in that baseline over a 5-year period given the course that we are on now?

Ms. RIVLIN. You are right, for government the baseline health care programs have come down. We did that to reflect what the actuaries told us about their extrapolation of the recent changes, that health care costs will grow less rapidly. But the costs are still growing rapidly. Nine percent is still a very rapid rate of growth.

There are several reasons for the change in the growth rate of health care costs. In Medicare, the growth rate has slowed primarily because hospital costs are not growing as rapidly. The slowdown in the growth of hospital costs reflects, in part, lower general inflation and, in part, greater efficiencies in the private sector.

Medicare's slower rate of growth does not have much to do with HMOs, however, because HMOs do not play a big role in Medicare.

With Medicaid, the change in the growth rate is due, in part, to the Federal Government having closed down the devices that the States were using to load more Medicaid expenses on the Federal Government. Everybody is struggling with these costs, and the States had been using various devices to load more of the costs on the Federal Government. The changes in the law enabled us to stop much of that from happening.

Mr. PAYNE. Are we now on a track where HCFA is likely in the next 5 years to come back, relook at this, and say that the rate of growth is even lower than what we are on now?

Ms. RIVLIN. I don't think we know the answer to that. We could hope that many of the changes that are going on in the private sector would be reflected, in part, in the government costs. I do think, however, that we need to look at Medicaid and Medicare in the context of overall health care reform and see if we can ensure a lower rate of growth in the future.

Mr. PAYNE. Thank you very much.

Mr. HOUGHTON. Thank you.

Mr. Portman.

Mr. PORTMAN. I thank the chairman. Dr. Rivlin, thank you for your willingness to stick it out here; your stamina is impressive. I think I am the last questioner you have to deal with.

I want to put a plug in quickly for unfunded mandate reform. Sally Katzen, a senior member of your staff, has been working with us closely on the conference; and I would hope the administration would support a meaningful proposal coming out of the conference.

The House bill, as you may know, was passed with an overwhelming majority; I think two-thirds of the Democrats in the end supported it. We would have liked to have had your support on that legislation and on the amendments, and we understand you are generally supportive. We hope to have the strongest bill possible coming out of conference after a 360-to-70 vote in the House of Representatives. Again, Ms. Katzen is to be commended for her work and interest in this.

Ms. RIVLIN. I am glad to hear this, and the administration is supportive of the unfunded mandates legislation.

Mr. PORTMAN. I am pleased to hear that. I would say, just in general, in listening to not only testimony but the questions and answers today, my largest concern is of course that the administration has not aggressively approached the deficit with this budget.

I looked at your objectives even before you came here today—and you have repeated them many times, including recently with Mr. Payne, that a better standard of living for the future—higher wages, those objectives are of course entirely consistent with aggressive deficit reduction as you have in a former life emphasized.

You talked about the problem you found in 1993, I think your quote was something like the use of the Nation's savings to finance the debt and the deficit led to a crisis situation that you came into in 1993. Again, I would say that both your objectives, as so stated in the budget and your analysis of 1993, would lead to very aggressive deficit reduction. I just don't see it here.

Two things in particular concern me about that. One is, this was your last chance. This was the last administration budget that you would have full control over, conceivably; and second, as the vice chairman of the committee, Mr. Gibbons has pointed out, this is the time to do it. We have relatively good economic times.

You talked about the recession after the 1990 budget deal and the impact that had on revenues and, therefore, the increase in the deficit. Well, now we have just the opposite situation. I hoped that the administration would have been far more aggressive in approaching the deficit. We talked about specifically your response being that as a percentage of the GDP, the deficit is not increasing. One figure I haven't heard yet, and I just wonder if you could answer quickly, is what is the percentage of GDP that the debt would represent over the next 5 years?

Ms. RIVLIN. While somebody is getting me that, let me comment on some of your other points.

I don't think this budget is our last chance or your last chance for deficit reduction. We will be working with the Congress not only on the budget, but on other items which are important to bringing the deficit down. One of those items is health care. We have put together a budget which contains aggressive cuts in discretionary spending. They don't get much attention up here, but we believe we have taken drastic steps to come up with proposals that would give us a leaner and more effective government. The deficit-reducing measures in this budget certainly move toward that direction.

Mr. PORTMAN. My question specifically would be, what does the debt—as a percentage of GDP, does that percentage figure also decline over the next 5 years and through the 10-year cycle?

Ms. RIVLIN. It stays about even.

Mr. PORTMAN. About even. You said in response to your questioning with Mr. Ford that both the deficit and the debt were being reduced over time as a percentage of GDP. So I think that is a significant figure. It is one that a lot of members have focused on, but we haven't heard the specific numbers. It is, I think, over——

Ms. RIVLIN. It is approximately flat.

Mr. PORTMAN. OK. After the 5 years you have about $70 billion per year in addition to the roughly $200 billion per year in debt service, of course.

Mr. ENSIGN. Would the gentleman yield?

Mr. PORTMAN. If the chair will indulge.

Mr. ENSIGN. Just real quickly, you may want to check with Secretary Rubin. He said the other day that it would also decrease.

Ms. RIVLIN. Well, logically it must, so I want to look at these figures. If the deficit is not rising as fast as the GDP, the debt must not be, either.

Mr. PORTMAN. It would depend on whether GDP increases over $1 trillion in the next 5 years. It seems to me that would be the key.

Will the chair indulge one more specific question?

Mr. HOUGHTON. Sure. You bet.

Mr. PORTMAN. Again in that context, I just wanted to ask you briefly on the Medicare front, that is a program under the jurisdiction of this committee, one we will be grappling with. I have looked at your testimony, you have talked about the rapid growth—you have talked about the fact that Medicare and Medicaid will double in the next 8 years from 3.4 percent of GDP to almost 5 percent in 10 years. Those two together are 40 percent of the increase in total outlays in the next 5 years.

Can you tell me what Medicare alone is as a percentage of the increase in the deficit over the next 5 years?

Ms. RIVLIN. I can certainly supply that figure for the record. But Medicare and Medicaid together are really the only items in the budget that are increasing rapidly. Medicare accounts for a significant increase in any future growth of spending.

Mr. PORTMAN. A substantial majority of that is Medicare, of course, in the next 5 years?

Ms. RIVLIN. Right.

Mr. PORTMAN. The absolute figures for the next 5 years for Medicare spending alone are roughly $1.2 trillion?

Ms. RIVLIN. We can supply that figure very easily.

Mr. PORTMAN. I think that figure, $1.2 trillion was something that came up in the Budget Committee testimony in absolute terms. It is over 9 percent per year increase in Medicare, and I would just say again, if you are going to get aggressive about deficit reduction, which I know you believe in and you have been a champion for in the past, not touching Medicare, it seems to me, is not a responsible approach.

You made the point again with Mr. Johnson that you didn't believe that there should be any reform of Medicare. We are not talking about cuts, remember, we are talking about reducing cost increases. You said that there shouldn't be any reforms of Medicare because we don't use Medicare to offset tax cuts—I think you said "for the rich," but even tax cuts, I think, are not intellectually honest. Certainly you could have had Medicare reform in here and had the other savings that you mentioned in the discretionary account for your tax reform measures. I would hope that the administration would be going to work with us not in the long term on health care reform, but in the short term on deficit reduction because it is such a huge part of the deficit problem. You are more familiar with that probably than anyone in this town, and I would have hoped that you could have come up with some specific ideas—whether it is means testing, whether it is increasing copayments, whether it is more HMOs, more managed care, whether it is just larger systemic change in the Medicare system, which clearly is out of control in terms of the 9-percent-per-year cost increases.

So my final point—Mr. Chairman, I appreciate the indulgence—is just to say that I hope that you wouldn't put that off until some possible health care debate in the future which may be very limited to insurance reform.

Ms. RIVLIN. We don't want to put it off. We do want to look at Medicare and Medicaid in the context of reforming the whole health care system. We did that last year. But Congress didn't exactly like what we did. We believe, however, that reforming Medicaid and Medicare has to be done with a view toward reforming the whole health care system. If we just reform Medicare and Medicaid, by cutting the programs and passing the costs on to the private sector, that won't do anybody any good.

Mr. PORTMAN. Well, I would disagree with that. I think the cost shifting involved in cutting reimbursements is one way to approach it. That is how you chose to approach it last year. There are lots of other more creative ways to do so, and again I think even when you talk to the administration about health care reform, people seem to be focused on the insurance reforms. There is nothing at all inconsistent with systemic change in the Medicare program, which again is under this concern, and I would hope that we could work together on that.

Thank you, Mr. Chairman.

Mr. HOUGHTON. Thank you, and thank you, Dr. Rivlin. You are a distinguished public servant. We thank you for your time. The committee will be in recess until 1 p.m.

Ms. RIVLIN. Thank you, Mr. Chairman.

[Whereupon, at 12:04 p.m., the committee recessed, to reconvene at 1 p.m. the same day.]

[Recess.]

Chairman ARCHER. This afternoon I believe we will complete our testimony on the President's budget and, looking at the number of the people in the room, apparently people have lost interest in the budget that has been submitted by the President. I am delighted to have you before our committee, and I think all of us realize this could be your final appearance before the committee.

We are particularly aware of that and also aware of the really fine service that you have given your country over the years, particularly through that most difficult exercise of all, the health care revisions last year. CBO has continued to serve Congress in their new roles and I feel certain that whatever your new role is, we will be hearing from you again.

So with great respect, welcome to the committee and we will be pleased to hear your testimony. As usual, anything you want to tell us verbally, go right ahead. If you have got something in writing that is longer, that will be submitted in full for the record.

STATEMENT OF ROBERT D. REISCHAUER, PH.D., DIRECTOR, CONGRESSIONAL BUDGET OFFICE

Mr. REISCHAUER. Thank you very much, Mr. Chairman.

I think this is my last testimony before a congressional committee as the Director of the Congressional Budget Office, and it is fitting in a way to appear with this committee that I have worked with very closely over the last 6 years. I hope to continue to have a close relationship with you when I am in the outside world.

I appreciate the opportunity to appear before you here this afternoon. With your permission, I will submit my prepared testimony for the record.

I will briefly compare CBO's latest views of the committee and the budget proposal of the administration and then I am going to describe to you the challenges involved in balancing the budget by the year 2002, which could be required if the Constitution is amended along the lines that were called for in the Joint Resolution that was adopted by the House on January 26.

With respect to the economy, CBO expects the strong growth that we experienced through 1994 to continue only slightly abated in the first half of this current year. Because the economy is operating at close to its potential, that growth is going to increase inflationary pressures a bit. But as a result of the monetary tightening that the Federal Reserve has engaged in over the last year, and any further monetary restraint that might be imposed, we believe that the economy will begin to slow down in the second half of 1995 and slow further in 1996.

On a fourth-quarter over fourth-quarter basis, real economic growth was 4 percent in 1994, and CBO expects growth to slow to 2.5 percent this year and then to 1.9 percent in 1996. The administration expects growth this year to be marginally slower than CBO does, but it expects growth in 1996 to be at about 2.5 percent or 0.6 of a percentage point faster than is projected in the CBO forecast.

Over the longer run, and by that I mean from 1997 through the year 2000, the administration projects that the economy will grow at 2.5 percent a year in real terms. That is about 0.2 of a percentage point faster than we had built into our economic projections. CBO expects the unemployment rate to average about 5.5 percent during the current year, 1995, and then to edge up a bit to 5.7 percent in 1996 as the economy begins to slow down.

The administration expects the unemployment rate to be at about 5.8 percent this year. In other words, a little bit higher than we do, and also following the path that we had suggested to tick up another 0.1 of a percentage point in 1996. The estimates of the unemployment rate that we have built into our forecast and that the administration has built into its forecast are all above the CBO estimate of 6 percent of the rate of unemployment that is compatible with nonaccelerating inflation.

In other words, we think the economy is operating a little bit above capacity and that will generate additional inflationary pressures.

Chairman ARCHER. Bob, if I may interject right there, do you mean the unemployment rate is actually going to be lower rather than higher than the 6-percent unemployment?

Mr. REISCHAUER. CBO's estimate of the unemployment rate that is compatible with inflation not beginning to increase is about 6 percent. Economists will disagree on that. Since we are projecting that the unemployment rate this year will be only around 5.5 percent, next year will go up to 5.7 percent. That means inflationary pressures——

Chairman ARCHER. What I wanted to clear up, I think you used the adjective "higher," and I think really it will be lower; will it not?

Mr. REISCHAUER. I am sorry, the unemployment rate will be lower than this nonaccelerating rate.

Chairman ARCHER. Thank you.

Mr. REISCHAUER. I am sorry if I misspoke.

Although inflation has been quite subdued over the past 2 years, it has been perking along at about 2.8 percent, CBO expects that the CPI will pick up modestly to 3.2 percent this year and then to 3.4 percent in 1996 as a result of the low unemployment rates that we were discussing. The administration expects the CPI to rise in 1995 at about the same rate that the Congressional Budget Office expects, but thereafter its inflation outlook is a bit more optimistic.

By the end of the decade, the administration has the CPI growing at 0.3 of a percentage point slower each year than does the Congressional Budget Office. Both CBO and the administration expect interest rates to rise this year and then fall a bit in 1996 as the economy slows. CBO expects higher short-term rates but lower long-term rates than the administration does.

Over the 1997–2000 period, the administration expects somewhat higher interest rates and lower unemployment rates than does CBO. Both the CBO and administration forecasts imply that the Federal Reserve's effort to restrain the economy will slow it down without causing a recession. Other outcomes are possible.

This is a very uncertain business. If the economy overshoots its potential by a wider margin than CBO expects, the Federal Reserve could take more drastic action that could presage a recession next year or in the following year. Alternatively, the rise that we have already experienced in interest rates could have been sufficient to slow the economy down, so we could have a very slow economy over the next few years.

Our forecast is really a compromise between these two different outlooks. With respect to the budget outlook, CBO expects the deficit in the current fiscal year to fall to $176 billion or 2.5 percent of GDP, gross domestic product, in dollar terms. That is going to be the lowest deficit we have experienced since 1989. In terms of a percent of GDP, it will be the lowest figure we have experienced since 1979; in other words, a full 16 years.

If further policies are not adopted to reduce the deficit, the 3 consecutive years of declining deficits that we have enjoyed will come to an end and the deficit will begin to rise in 1996. The mounting deficits will be fueled primarily by increases in Medicare and Medicaid, which we expect to grow by about 10 percent a year; CBO projects that all spending other than that for Medicare and Medicaid will grow at only about half that rate.

By 2005, the deficit is projected to reach $421 billion or 3.6 percent of GDP if one assumes that discretionary spending is adjusted for inflation after the discretionary caps expire in 1998. The administration is more sanguine about the baseline budget outlook; that is, the budget outlook that will occur under a continuation of current policies rather than under the tax and spending changes that have been recommended in the President's budget.

For the current fiscal year, the administration expects the baseline deficit to be $17 billion higher than does CBO, $193 versus $176 billion. However, it expects the baseline deficit to be lower than CBO's estimates by growing amounts over the 1996–2000 period. In fact, the administration's estimate for the deficits under a continuation of current policy is some $55 billion below CBO's estimates by the year 2000. All told, the administration expects baseline deficits over the 1996–2000 period to be $112 billion lower than does CBO.

The administration projects that baseline discretionary spending will be about $36 billion higher during the next 5 years than does CBO. The difference arises primarily because the administration has used a different method to adjust the discretionary spending caps for unanticipated inflation, and in the questions I can pursue that issue if you have any interest in that.

During the 1996–2000 period, the administration expects over $70 billion more in baseline revenues than does CBO. The difference is largely attributable to the administration's higher projections of nominal GDP. The administration's estimates for Medicare and Medicaid spending over the 1996–2000 period are about $70 billion less than CBO's estimates. The administration expects these programs to grow at a rate of about 1 percentage point slower than does CBO.

The comparisons I have been discussing relate to the budget outlook under a continuation of current policies, and, Mr. Chairman, CBO will be analyzing the policy proposals that the President has put forward and will be issuing a report to the Congress some time in early March.

Let me turn to the last issue.

Chairman ARCHER. Bob, can I ask you to suspend? I am sorry to do this. I only have a little time to get over and vote. With your indulgence, I am going to vote and the first Republican that comes back will continue the hearing until I can get back.

Mr. REISCHAUER. Fine.

[Recess.]

Mr. CHRISTENSEN [presiding]. Mr. Reischauer, you want to continue? This might be the only time I get to do this.

Mr. REISCHAUER. Let me say, Mr. Chairman,——

Mr. CHRISTENSEN. About 30 years from now, maybe?

Mr. REISCHAUER. I think whoever sits in the seat is Mr. Chairman.

Let me turn now to the last question that I said I would talk about, which is what it would take to balance the budget by the year 2002. What would be required if the constitutional amendment passes and is approved by three-quarters of the States? According to CBO's projections, some combination of spending cuts, tax increases, and reduced debt service that total $322 billion in the year 2002 would be needed to eliminate the deficit in that year. There are many possible paths to that objective, one of which I have laid out on the last page of my prepared statement.

In that particular path we have first frozen discretionary spending through the year 2002 at the level of the 1998 cap. That action, together with the resulting debt service effects, would produce $89 billion of the $322 billion in savings that is needed to balance the budget by 2002.

If we were to pursue that policy, the buying power of the discretionary appropriations in 2002 would be about 20 percent less than it is in 1995. The illustrative path toward a balanced budget next assumes further savings from policy changes, the pattern of which is similar to that of the mandatory program savings that were contained in the reconciliation bills of 1990 and 1993. If these savings were achieved entirely out of entitlement and other mandatory programs, but we exempted Social Security, they would represent about a 20-percent reduction from the current policy levels for those programs.

The responsibility for making those types of cuts, of course, would fall largely to this committee. Looking over the period from 1996–2002, the savings in the CBO illustrative path that result directly from policy changes total more than $1 trillion and the associated debt service savings amount to about $175 billion, but this picture probably overstates the severity of the policy-related cuts that would be needed to balance the budget.

If the necessary policies were enacted into law soon and financial markets were convinced that policymakers would stay the course, CBO expects that interest rates would fall below those that are contained in its forecast. This would increase the debt service savings and reduce the amount of savings needed from policy changes.

If interest rates were to fall by as much as 1 percentage point below the levels that are assumed in the CBO forecast for the year 2002—and this, I think, is a plausible order of magnitude of the possible reduction in interest rates—the amount of savings that would be needed from policy changes over the 7-year period to balance the budget would be almost $140 billion less than the $1.035 trillion that are shown in the last table of my handout.

Lest I sound too negative, let me remind you that there are significant, long-run economic benefits to be gained from reducing the deficit. Productivity would increase. Living standards would rise.

We would be less dependent on foreigners for future investment funding and our debt-to-GDP ratio would begin to decline. But the road to a balanced budget will be one we have never traveled before. It would involve sustained fiscal restraint that would average about 0.4 of a percentage point of GDP each year and that would have a contractionary effect on the economy.

To some degree, that contractionary impact would be offset by lower interest rates that would result from the reduction in Federal credit demands and some possible monetary easing by the Federal Reserve. It would also be offset by stronger exports that would be brought on by reduced exchange rates. Nevertheless, there could be a few bumps along the road that I have laid out.

Let me conclude by noting that the magnitude of the discretionary and mandatory cuts contained in the illustrative path to a balanced budget are large but they are not unattainable. Their size could be reduced, of course, if tax increases were considered as part of the equation.

If taxes are reduced, on the other hand, deeper spending cuts will be required. These are the issues that this committee will play a major role in deciding and they will determine the future course of our fiscal policy.

With that, let me conclude. I will be happy to answer any questions that members of the committee might have.

[The prepared statement and attachments follow:]

STATEMENT OF ROBERT D. REISCHAUER DIRECTOR, CONGRESSIONAL BUDGET OFFICE

Chairman Archer, Congressman Gibbons, and Members of the Committee, I am pleased to be with you this afternoon to review the state of the economy and the budget. Last week, the Congressional Budget Office (CBO) published *The Economic and Budget Outlook: Fiscal Years 1996-2000*, which describes our current views in considerable detail. My testimony summarizes that report. It also briefly compares CBO's outlook with the economic forecast and budget projections in the President's budget released earlier this week.

No fundamental change in the economic or budget situation has occurred since CBO published *The Economic and Budget Outlook: An Update* in August 1994. The economy may be a bit more robust in 1995 than had been anticipated at that time, but a likely slowdown in growth in 1996 leaves the long-term economic outlook little different from last summer's. CBO expects that the high levels of business investment and purchases of durable goods that spurred the economy to a 4.0 percent real rate of growth in 1994 will continue into the first part of 1995. Because the economy is already operating close to its potential (the level of gross domestic product, or GDP, consistent with a stable rate of inflation), that growth is expected to result in somewhat higher rates of inflation and interest. In turn, those higher interest rates are likely to slow growth by the end of 1995--cutting it to 2.5 percent in 1995 and 1.9 percent in 1996 and dampening inflationary pressures. In CBO's longer-term projections, average annual growth after 1996 is close to the 2.4 percent rate of growth estimated for potential GDP; over the 1997-2000 period covered by those projections, inflation averages 3.4 percent and interest rates drift down.

CBO projects that the deficit will decline from the $203 billion registered in 1994 to $176 billion in 1995, the lowest level since 1989 and the lowest as a percentage of GDP (2.5 percent) since 1979. After reaching a trough in 1995, the deficit will rise to $207 billion in 1996 (2.8 percent of GDP), grow again in 1997, and then level off in 1998. Those projections assume no change in current policies governing taxes and mandatory spending; they also assume compliance with the limits on discretionary appropriations that are in place through 1998. Under the assumption that spending for discretionary programs increases at the rate of inflation after 1998, deficits will grow to $284 billion (3.1 percent of GDP) in 2000, the last year of CBO's regular projections. Under an alternative baseline that assumes that discretionary spending remains frozen at the dollar level of the 1998 caps, deficits increase only to $243 billion in 2000.

CBO's extended projections for 2001 through 2005, which are less detailed than those through 2000, show deficits continuing to mount in dollar terms through 2005 if discretionary spending is adjusted for inflation after 1998 (see Figure 1 at the end of this statement). Deficits also grow as a percentage of GDP--to 3.6 percent in 2005. There is no reason to believe that this trend will be reversed in the years after that; indeed, the growth in the deficit is likely to accelerate in the second decade of the 21st century as large numbers of baby boomers become eligible for Social Security and Medicare benefits. Extended baseline projections that assume that discretionary spending is frozen at the 1998 level show deficits that are nearly constant from 2000 through 2005. As a percentage of GDP, the deficit in that baseline shrinks from 2.7 percent in 1998 to 2.1 percent in 2005.

Higher-than-anticipated interest payments and lower revenues, which are only partially offset by lower spending for medical care programs, have pushed up CBO's deficit projections for fiscal years 1995 through 1999 from last August's estimates by an average of almost $25 billion a year. After 2002, however, the deficits in the new extended projections are a little lower than the deficits projected in August.

The Administration's economic assumptions are not dramatically different from CBO's, but its baseline deficit projections for fiscal years 1995 through 2000 (generally based on the assumption that current laws and policies are unchanged) are almost $100 billion lower than those of CBO. It will take several weeks to analyze the President's budget thoroughly, but a quick assessment suggests that seemingly small differences in economic assumptions are likely to account for a significant amount of the discrepancy between CBO's and the Administration's baseline deficit estimates. Divergent estimates of discretionary spending and expenditures for Medicare and Medicaid also contribute to the difference in deficit projections.

The Congress is considering a constitutional amendment, which could go into effect as early as 2002, requiring a balanced budget. CBO currently projects a deficit of $322 billion for that year (assuming that discretionary spending is adjusted for inflation after 1998), which is only $3 billion more than the amount estimated last August. To illustrate the magnitude of the task facing those who would have to enact policies to comply with the balanced budget requirement, CBO has constructed an illustrative path leading to a balanced budget in 2002 that entails deficit reduction of $1.2 trillion over the 1996-2002 period. Major changes in current policies would be required to achieve deficit reduction on that scale.

THE ECONOMIC OUTLOOK

CBO forecasts that the strong economic growth that the nation experienced throughout 1994 will continue into the first part of 1995. Because the economy is operating close to its potential, that growth will increase inflationary pressures and is likely to trigger additional efforts by the Federal Reserve Board to rein in the economy with higher short-term interest rates. In the CBO forecast, the resulting moderate slowdown at the end of 1995 and during 1996 will gradually bring GDP back in line with potential output without seriously disrupting the economy. Even with somewhat higher short-term growth and the slowdown in 1996, the current economic projections for 1997 through 1999 are little different from those CBO made last August.

The Forecast for 1995 and 1996

The robust growth that the U.S. economy experienced in 1994 is likely to continue through the first part of 1995 but will fade by the end of the year. The 4.0 percent increase in real output (on a fourth-quarter-to-fourth-quarter basis) and the creation of over 3 million new jobs in 1994 were achieved without an increase in inflation, but that performance is not likely to be repeated in 1995 (see Table 1). Because the economy is already operating close to its potential, it cannot persistently expand faster than the growth of potential output--estimated at 2.4 percent a year by CBO--without triggering modestly higher inflation.

The Federal Reserve, which is determined to avoid any significant increase in inflation, raised the federal funds rate by 250 basis points (2.5 percentage points) in 1994 and boosted it an additional 50 basis points last week. CBO forecasts that 90-day Treasury bill rates will average 6.2 percent in 1995--up from 3.2 percent in the first quarter of 1994. Rates for 10-year Treasury notes are expected to increase more modestly. The high rates of business investment and personal consumption of durable goods that drove the economy forward in 1994 apparently have not yet declined and will keep growth strong in the first part of 1995. However, by 1996, the cumulative effect of past and future hikes in interest rates should begin to bring the economy back in line with potential output. As a result, CBO expects that growth of real GDP will slow to 1.9 percent in 1996.

Unemployment will remain low in 1995--it is forecast to average 5.5 percent, compared with 6.1 percent in 1994--but will climb to 5.7 percent in 1996. Even at 1996's slightly higher level, unemployment will be below CBO's estimate of 6.0 percent for the nonaccelerating inflation rate of unemployment (NAIRU). A sustained unemployment rate below the NAIRU indicates a future increase in wage inflation. With unemployment below the NAIRU and GDP exceeding potential output, inflation is expected to rise in 1995 and 1996. Because the economy has not become too overheated and is expected to cool down later this year, the forecast upswing in the consumer price index for all urban consumers (CPI-U) is modest--from 2.7 percent in 1994 to 3.2 percent in 1995 and 3.4 percent in 1996 (see Table 1).

CBO's forecast assumes that the recent and anticipated future increases in short-term interest rates engineered by the Federal Reserve will restrain the economy to an appropriate degree. If the continuing strong growth that CBO foresees in early 1995 does not take place--if the economy has already started to cool off--the expected additional monetary tightening will slow growth sooner and more sharply than anticipated. Alternatively, if the economy proves stronger and more resistant than expected to the anticipated increases in interest rates and it surges well above potential output, the Federal Reserve will probably respond with even higher interest rates to combat the risk of inflation. That stronger-than-expected growth and the Federal Reserve's response to it could usher in a cycle of boom and bust for the economy.

Some economists argue that potential output may be greater than CBO estimates, in which case the economy could grow at its current rate for some time without triggering higher inflation. The Federal Reserve, however, is unlikely to allow such growth unless the evidence for a shift in potential output is more compelling than it currently is.

The Administration foresees somewhat slower real growth during 1995 than does CBO, but does not forecast as much of a slowdown in 1996. Compared with CBO's forecast, the Administration assumes the consumer price index rises more rapidly in 1995 and more slowly in 1996; the implicit GDP deflator rises faster in both years. Interest rates on three-month Treasury bills are lower in the Administration's forecast, but rates on 10-year Treasury notes are higher. The Administration's unemployment rate is higher in both 1995 and 1996.

Projections for 1997 Through 2000

CBO attempts to forecast the cyclical fluctuations in the economy only for the next two years. Beyond 1996, its projections are based on trends in fundamental factors that determine the potential growth of the economy, including growth in the labor force, productivity, and national saving.

CBO's projections follow a path that has the gap between GDP and potential GDP reaching its historical average level--with GDP 0.6 percent below potential--at the end of the projection period in 2000. Because CBO estimates that the level of GDP will exceed potential output in 1996, the average annual real growth projected for 1997 through 2000 is slightly below the estimated 2.4 percent rate of growth of potential output (see Table 2). Unemployment is expected to increase slightly to 6.0 percent, the estimated level of the NAIRU. Projected consumer price increases are assumed to average 3.4 percent a year over the period, with projected interest rates declining from the levels associated with efforts to slow the economy in 1995 and 1996.

The Administration also assumes that real growth will average 2.5 percent a year in 1997 through 2000. It assumes that over that period the consumer price index will grow more slowly--less than 3.2 percent a year--than CBO projects, but that the implicit GDP deflator will increase at an average rate of 3.0 percent a year, higher than the 2.8 percent average annual increase projected by CBO. The Administration assumes a lower rate of unemployment in 1997 through 2000 but higher short- and long-term interest rates.

THE BUDGET OUTLOOK

Although CBO now projects that the deficits for fiscal years 1995 through 1999 will be almost $25 billion a year higher, on average, than it anticipated last August, the fundamental budget outlook is not very different from the one CBO projected then. Moreover, there has been no substantial change in CBO's deficit projections since its report in September 1993, which for the first time reflected the more than $400 billion in deficit reduction enacted in the Omnibus Budget Reconciliation Act of 1993 (see Figure 2). The deficit is still expected to fall in 1995 to its lowest level since 1989--and its lowest point as a percentage of GDP since 1979. As was also the case in August, the deficit is projected to begin rising again in 1996. CBO's extended budget projections show that trend continuing through 2005 if spending for discretionary programs increases at the rate of inflation after 1998. After 2002, currently projected deficits are slightly lower than the deficits forecast in August.

The Outlook for the Deficit

Since 1992's record-high shortfall of $290 billion, the deficit has declined to $255 billion (4.0 percent of GDP) in 1993 and $203 billion (3.1 percent of GDP) in 1994. (Although a record in dollar terms, the 1992 deficit as a percentage of GDP was far short--at 4.9 percent--of even a postwar record.) CBO projects that the deficit will decline for a third straight year to $176 billion (2.5 percent of GDP) in 1995 (see Table 3). That gratifying trend is expected to end next year, however, with the deficit climbing under current laws to $207 billion (2.8 percent of GDP) in 1996 and $224 billion (2.9 percent of GDP) in 1997 before leveling off in 1998.

The standardized-employment deficit, which is an estimate of the deficit that would occur if the economy was operating at its potential, is of interest because it is a measure of the fiscal posture of the federal budget without the cyclical effects of the economy. When the economy is operating below potential, the deficit swells as a result of reductions in revenues and increased spending for programs such as unemployment insurance. When the economy is operating above potential, revenues are increased and spending is lower. Because in CBO's forecast the economy will be operating close to potential throughout the 1995-2000 period, the projected standardized-employment deficits differ little from the projected total deficits. Despite that, a look at the standardized-employment deficit as a percentage of potential GDP is still illuminating. That measure varies only slightly from year to year during the 1994-1998 period, which makes it clear that the fiscal stance of the budget changes hardly at all during that time.

CBO's baseline projections for mandatory spending programs and taxes represent the outlays and revenues that will result if no changes are made in the laws governing those parts of the budget. The projections for discretionary spending (spending controlled by annual appropriations) assume compliance with the discretionary spending limits for 1996 through 1998 established for general-purpose appropriations in the Balanced Budget and Emergency Deficit Control Act of 1985 and for specific anticrime appropriations in the Violent Crime Control and Law Enforcement Act of 1994. Because no level of discretionary spending is set by law for the years after 1998, CBO makes two different projections of the deficit for 1999 and later years. In one projection, discretionary spending grows at the rate of inflation; the purchasing power of the appropriations is thus held constant at the 1998 level. In the other, discretionary spending is frozen at the 1998 dollar level.

In the baseline projections with discretionary spending adjusted for inflation after 1998, the deficit resumes its upward path after the pause in 1998. By 2000, the last year of CBO's regular projections, the deficit of $284 billion is almost back to the record level of 1992 (although at 3.1 percent, it is well below the 1992 deficit as a percentage of GDP). CBO's extended projections show deficits that continue to climb after 2000, reaching $421 billion (3.6 percent of GDP) in 2005. The mounting deficits continue to be fueled primarily by increases in Medicaid and Medicare, even though projected costs for those programs are somewhat lower than CBO had estimated last August. All spending other than that for Medicaid and Medicare is projected to grow at an average rate of about 5 percent a year between 1998 and 2005, slightly slower than the rise in revenues. Projected spending for the two big federal health programs, however, increases at an average rate of almost 10 percent a year after 1998.

In the baseline projections without inflation adjustments for discretionary spending after 1998, deficits level off at around $240 billion a year from 1999 through 2005. (The projected deficit of $242 billion for 2005 is equal to 2.1 percent of GDP.) Freezing discretionary appropriations at the 1998 dollar level through 2005 would result in funding for discretionary programs in 2005 that had about 27 percent less purchasing power than the 1995 appropriations. If total discretionary spending was frozen at the nominal 1998 level but defense spending was preserved at the 1995 funding level adjusted for inflation, the money available for all other discretionary programs in 2005 would have less than half the purchasing power of the 1995 appropriations for those programs.

All mandatory spending is the same in both baselines, except that interest payments reflect the lower deficits and debt in the version that does not adjust discretionary spending for inflation after 1998.

The Administration's baseline deficits are almost $100 billion less over the 1995-2000 period than the deficits in CBO's baseline with discretionary inflation after 1998 (see Table 4). The 1995 deficit is $17 billion higher than CBO projects, but in every other year the Administration's estimate is lower--in fact, by as much as $55 billion in 2000. The Administration's baseline concept is similar to CBO's, but differences between the Administration's and CBO's method of adjusting the discretionary caps for inflation account for the Administration's projection of baseline discretionary spending that is as much as $9 billion higher than CBO's in 1998. The Administration projects that revenues under current law will be more than $60 billion higher than CBO estimates in 1995 through 2000. A significant part of that difference is the result of the higher levels of nominal GDP projected by the Administration. The Administration also projects outlays for Medicare and Medicaid that are around $70 billion lower than CBO estimates for 1995 through 2000. CBO's detailed analysis of the President's budget, which should be available in March, will provide a much more thorough explanation of the differences between the Administration's and CBO's projections than we can give now based on our initial look at the budget.

According to the Administration, the policies proposed in the President's budget would reduce the deficits over the 1995-2000 period by about $80 billion, with $136 billion in spending cuts more than offsetting a $56 billion reduction in revenues. CBO's analysis of the President's budget will include CBO's estimate of the effects of the policies proposed by the Administration. However, we are not yet able even to hazard a guess about whether our estimate will be significantly different from the Administration's.

Changes in the Projections

The deficits that CBO currently projects for 1995 through 1999 are almost $25 billion a year higher, on average, than those projected last August (see Table 5). Yet despite those increases, there has been no fundamental change in the deficit outlook. In fact, by 2003, the deficits in CBO's current extended projections are slightly lower than the deficits CBO projected in August.

Legislation enacted since then has had very little effect on the deficit outlook. The two most significant laws were an act making major changes in the federal crop insurance program in hopes of avoiding future ad hoc disaster assistance to farmers and an act implementing the Uruguay Round of the General Agreement on Tariffs and Trade (GATT). The crop insurance legislation increased estimates of the deficit by almost $1 billion a year. Because CBO's baseline projections were made on the basis of current law, they did not include any spending that might result from the enactment of future ad hoc disaster bills. Therefore, reducing the likelihood of such legislation did not produce savings that could offset the higher spending for crop insurance. The GATT implementing legislation added almost $3 billion to deficits over the 1995-1999 period because losses in revenues from lower tariffs were not completely offset by other revenue increases and spending cuts.

Changes in the economic forecast since August have had a greater effect on deficit projections than has legislation. Economic changes have pushed down projected revenues by $9 billion in 1996 and $8 billion in 1997, largely because of lower wage and salary income than had been forecast in August. More significantly, the higher interest rates in the new forecast have driven up projected federal interest payments by more than $15 billion a year, on average, in 1996 through 1999.

Taken altogether, technical reestimates--those changes that cannot be attributed to legislation or revisions in the economic forecast--have had little impact on projections of the deficit. But looking only at the total effect masks some significant changes. Projected Medicaid spending is lower in every year--by as much as $13 billion in 1999--than was estimated in August, reflecting actual 1994 outlays that were lower than expected and evidence that the rapid growth in that program has slowed. Medicare expenditures are down only slightly over the 1995-1999 period, but CBO's extended forecasts have significantly lower spending for Medicare as well as Medicaid in the years after 2000. The Medicaid reductions in 1995 through 2000, however, are more than offset by technical reestimates that bring down projected revenues to reflect smaller-than-anticipated tax collections in 1994 and increased spending for a variety of programs other than Medicare and Medicaid.

ILLUSTRATIVE PATH TO A BALANCED BUDGET

A constitutional amendment requiring a balanced federal budget will be considered during the early days of the 104th Congress. If the Congress adopts such an amendment this year and three-quarters of the state legislatures ratify it over the next few years, the requirement could apply to the budget for fiscal year 2002. If the budget is to be balanced by 2002, it is important that the Congress and the President begin immediately to put into effect policies that will achieve that goal. According to CBO's latest projections of a baseline that adjusts discretionary spending for inflation after 1998, some combination of spending cuts and tax increases totaling $322 billion in 2002 would be needed to eliminate the deficit in that year. The amounts of deficit reduction called for in the years preceding 2002 depend on both the exact policies adopted and when the process is begun.

For illustrative purposes, CBO has laid out one of many possible paths to a balanced budget in 2002 (see Table 6). Starting from a baseline that assumes that discretionary spending is adjusted for inflation after 1998, that path first shows the savings that would be achieved by freezing discretionary spending through 2002 at the dollar level of the 1998 cap. Such a freeze, along with the resulting debt-service effects, would produce $89 billion of the required savings of $322 billion in 2002. Under the freeze policy, the buying power of total discretionary appropriations in 2002 would be approximately 20 percent less than in 1995.

CBO also built into its illustrative path a possible course of savings from further policy changes. The amounts of those savings are not based on the adoption of any particular set of policies; they do assume, however, that policy changes are phased in between 1996 and 1999 in a pattern that is similar to the changes in mandatory spending enacted in the last two major efforts at deficit reduction in 1990 and 1993. After 1999, the assumed savings increase at the baseline rate of growth for entitlement and other mandatory spending, excluding Social Security--implying that the cuts implemented in earlier years have a permanent effect but no additional policy changes have been made. If those savings were achieved entirely out of entitlement and other mandatory programs (excluding Social Security), they would represent about a 20 percent reduction from current-policy levels for those programs.

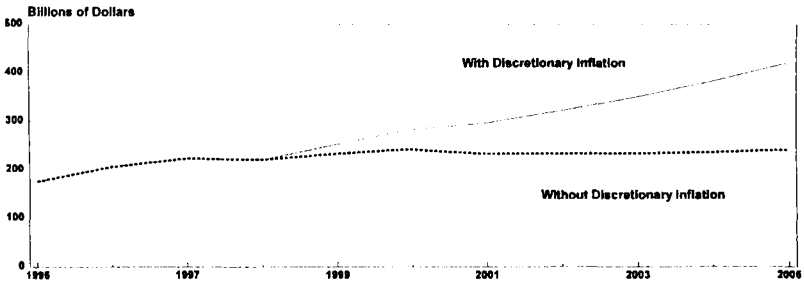
Over the entire 1996-2002 period, the savings in CBO's illustrative path that result directly from policy changes total more than $1 trillion (in relation to a baseline that adjusts discretionary spending for inflation after 1998). When the resulting savings in debt-service payments are included, the total exceeds $1.2 trillion. As noted, this path and the resulting $1.2 trillion in savings are illustrative only; the actual amount of cumulative deficit reduction over the 1996-2002 period will depend on the timing and exact nature of the policies enacted to achieve balance in 2002.

The required savings from policy changes would be smaller and the debt-service savings greater if, as CBO anticipates, ongoing deficit reduction efforts over this period result in lower interest rates. CBO believes that by 2000, interest rates could be as much as 1 percentage point lower than it currently forecasts if spending cuts and tax increases that would lead to a balanced budget have been enacted and the financial markets are convinced that policymakers will maintain those policies. CBO estimates that such a drop in interest rates would lower projected federal interest payments--and the amount of savings from policy changes needed to balance the budget--by almost $140 billion over the 1996-2002 period.

CONCLUSION

CBO's most recent economic and budget projections underscore the challenge facing policymakers who may have to enact the spending cuts or tax increases needed to balance the budget by 2002. Although the long-term budget outlook is no worse now than it was last August, the new projections emphasize that the deficit can be eliminated only through major changes in current policies.

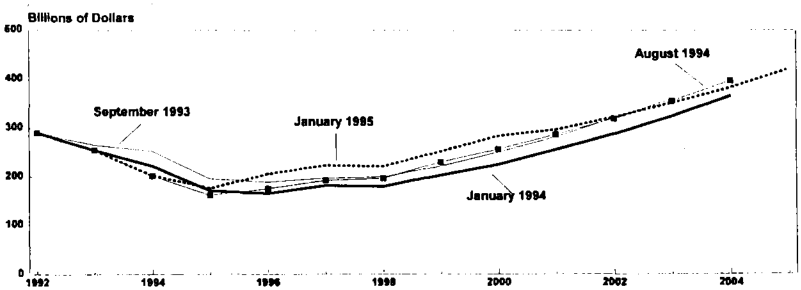
Figure 1.
Comparison of CBO Deficit Projections With and Without Discretionary Inflation After 1998 (By fiscal year)



SOURCE: Congressional Budget Office.

NOTE: Caps on discretionary spending are set by law through 1998. Measures of the deficit "with discretionary inflation" assume that discretionary spending grows at the rate of inflation after 1998. Measures of the deficit "without discretionary inflation" assume that discretionary spending remains frozen in dollar terms at the level of the 1998 caps.

Figure 2.
Comparison of CBO Deficit Projections (By fiscal year)



SOURCE: Congressional Budget Office.

NOTE: The projections assume that discretionary spending rises with inflation after the caps expire in 1998.

Table 1.
Comparison of Forecasts for 1995 and 1996

	Actual		Forecast	
	1993	1994	1995	1996
	Fourth Quarter to Fourth Quarter (Percentage change)			
Nominal GDP				
CBO	5.0	6.3	5.3	4.7
Administration	5.0	6.3	5.4	5.5
Blue Chip	5.0	6.3	5.7	5.4
Real GDP[a]				
CBO	3.1	4.0	2.5	1.9
Administration	3.1	4.0	2.4	2.5
Blue Chip	3.1	4.0	2.5	2.2
Implicit GDP Deflator				
CBO	1.8	2.3	2.8	2.8
Administration	1.8	2.3	2.9	2.9
Blue Chip	1.8	2.3	3.1	3.2
Consumer Price Index[b]				
CBO	2.7	2.7	3.2	3.4
Administration	2.7	2.7	3.3	3.2
Blue Chip	2.7	2.7	3.5	3.5
	Calendar Year Averages (Percent)			
Civilian Unemployment Rate				
CBO	6.8	6.1	5.5	5.7
Administration	6.8	6.1	5.8	5.9
Blue Chip	6.8	6.1	5.6	5.7
Three-Month Treasury Bill Rate				
CBO	3.0	4.2	6.2	5.7
Administration	3.0	4.2	5.9	5.5
Blue Chip	3.0	4.2	6.2	6.1
Ten-Year Treasury Note Rate				
CBO	5.9	7.1	7.7	7.0
Administration	5.9	7.1	7.9	7.3
Blue Chip[c]	5.9	7.1	7.9	7.6

SOURCES: Congressional Budget Office; Office of Management and Budget, *The Budget of the United States Government, Fiscal Year 1996*; Eggert Economic Enterprises, Inc., *Blue Chip Economic Indicators* (January 10, 1995); Department of Commerce, Bureau of Economic Analysis.

NOTE: The *Blue Chip* forecasts are based on a survey of 50 private forecasters.

a. Based on constant 1987 dollars.

b. The consumer price index for all urban consumers (CPI-U).

c. *Blue Chip* does not project a 10-year note rate. The values shown here for the 10-year note rate are based on the *Blue Chip* projections of the Aaa bond rate, adjusted by CBO to reflect the estimated spread between Aaa bonds and 10-year Treasury notes.

Table 2.
The Economic Forecast and Projections (By calendar year)

	Actual	Forecast		Projected			
	1994	1995	1996	1997	1998	1999	2000
Nominal GDP (Billions of dollars)	6,737	7,127	7,456	7,847	8,256	8,680	9,128
Real GDP (Billions of 1987 dollars)	5,342	5,505	5,602	5,736	5,870	6,004	6,141
Real GDP (Percentage change)	4.0	3.1	1.8	2.4	2.3	2.3	2.3
Implicit GDP Deflator (Percentage change)	2.1	2.6	2.8	2.8	2.8	2.8	2.8
CPI-U (Percentage change)[a]	2.6	3.1	3.4	3.4	3.4	3.4	3.4
Unemployment Rate (Percent)	6.1	5.5	5.7	5.8	5.9	6.0	6.0
Three-Month Treasury Bill Rate (Percent)	4.2	6.2	5.7	5.3	5.1	5.1	5.1
Ten-Year Treasury Note Rate (Percent)	7.1	7.7	7.0	6.7	6.7	6.7	6.7

SOURCE: Congressional Budget Office

a. CPI-U is the consumer price index for all urban consumers

Table 3.
CBO Deficit Projections (By fiscal year)

	1994	1995	1996	1997	1998	1999	2000
	In Billions of Dollars						
Baseline Total Deficit							
With discretionary inflation after 1998	203	176	207	224	222	253	284
Without discretionary inflation after 1998	203	176	207	224	222	234	243
Standardized-Employment Deficit[a]							
With discretionary inflation after 1998	187	200	216	223	221	247	273
Without discretionary inflation after 1998	187	200	216	223	221	228	233
	As a Percentage of GDP						
Baseline Total Deficit							
With discretionary inflation after 1998	3.1	2.5	2.8	2.9	2.7	3.0	3.1
Without discretionary inflation after 1998	3.1	2.5	2.8	2.9	2.7	2.7	2.7
Standardized-Employment Deficit[b]							
With discretionary inflation after 1998	2.8	2.8	2.9	2.9	2.7	2.9	3.0
Without discretionary inflation after 1998	2.8	2.8	2.9	2.9	2.7	2.6	2.6

SOURCE: Congressional Budget Office

NOTE: Caps on discretionary spending are set by law through 1998. Measures of the deficit "with discretionary inflation" assume that discretionary spending grows at the rate of inflation after 1998. Measures of the deficit "without discretionary inflation" assume that discretionary spending remains frozen in dollar terms at the level of the 1998 caps.

a. Excludes the cyclical deficit and spending for deposit insurance

b. Shown as a percentage of potential gross domestic product

Table 4.
CBO and Administration Budget Projections (By fiscal year, in billions of dollars)

	1995	1996	1997	1998	1999	2000
CBO's Baseline with Discretionary Inflation After 1998[a]						
Revenues	1,355	1,418	1,475	1,546	1,618	1,697
Outlays	1,531	1,625	1,699	1,769	1,872	1,981
Deficit	176	207	224	222	253	284
Difference from CBO's Baseline						
Revenues	-9	1	7	13	20	31
Outlays	8	-6	1	b	-12	-23
Deficit	17	-6	-6	-13	-32	-55
Administration's Budget Baseline[a]						
Revenues	1,346	1,418	1,482	1,560	1,638	1,729
Outlays	1,539	1,620	1,700	1,769	1,860	1,958
Deficit	193	201	218	209	221	229
Difference from Administration's Budget Baseline						
Revenues	b	-3	-10	-11	-14	-18
Outlays	b	-7	-15	-24	-37	-53
Deficit	b	-4	-5	-13	-24	-35
Administration's Budget Policy						
Revenues	1,346	1,415	1,472	1,549	1,625	1,711
Outlays	1,539	1,612	1,685	1,745	1,822	1,905
Deficit	193	197	213	196	197	194

SOURCES: Congressional Budget Office. Office of Management and Budget, *The Budget of the United States Fiscal Year 1996*

a. Assumes discretionary spending complies with caps through 1998 and grows at the rate of inflation after 1998

b. Less than $500 million.

Table 5.
Changes in CBO Deficit Projections (By fiscal year, in billions of dollars)

	1995	1996	1997	1998	1999
August 1994 Baseline Total Deficit with Discretionary Inflation After 1998	162	176	193	197	231
Changes					
Policy changes	2	2	2	3	3
Economic assumptions					
Revenues[a]	2	9	8	3	b
Net Interest	8	16	17	15	15
Other outlays	b	b	1	2	2
Subtotal	10	25	27	20	17
Technical reestimates					
Revenues[a]	6	5	6	9	11
Deposit insurance[c]	1	3	b	b	1
Medicaid and Medicare	-7	-6	-8	-11	-15
Net interest[c]	b	-1	b	b	1
Other outlays	b	5	4	3	5
Subtotal	1	5	2	2	2
Total	13	31	31	26	22
January 1995 Baseline Total Deficit with Discretionary Inflation After 1998	176	207	224	222	253

SOURCE: Congressional Budget Office

NOTE: Caps on discretionary spending are set by law through 1998. Measures of the deficit "with discretionary inflation" assume that discretionary spending grows at the rate of inflation after 1998.

a. Revenue reductions are shown with a positive sign because they increase the deficit.

b. Less than $500 million.

c. Excludes changes in interest paid by deposit insurance agencies to the Treasury. These interest payments are intrabudgetary and do not affect the deficit.

Table 6.
Illustrative Deficit Reduction Path (By fiscal year, in billions of dollars)

	1995	1996	1997	1998	1999	2000	2001	2002	1996-2002
CBO January Baseline Deficit with Discretionary Inflation After 1998	176	207	224	222	253	284	297	322	n.a.
Freeze Discretionary Outlays After 1998									
Discretionary reduction	0	0	0	0	-19	-38	-58	-78	-193
Debt service	0	0	0	0	-1	-2	-6	-10	-19
Total Deficit Reduction	0	0	0	0	-19	-40	-63	-89	-212
CBO January Baseline Deficit Without Discretionary Inflation After 1998	176	207	224	222	234	243	234	234	n.a.
Additional Deficit Reduction									
Policy changes[a]	0	-32	-65	-97	-145	-156	-168	-180	-843
Debt service	0	-1	-4	-10	-18	-28	-40	-54	-156
Total Deficit Reduction	0	-33	-69	-106	-163	-184	-208	-234	-998
Resulting Deficit	176	174	155	116	71	59	26	b	n.a
Total Change from Baseline Deficit with Discretionary Inflation After 1998									
Policy changes	0	-32	-65	-97	-164	-194	-225	-259	-1,035
Debt service	0	-1	-4	-10	-19	-31	-46	-64	-175
Total Deficit Reduction	0	-33	-69	-106	-182	-225	-271	-322	-1,210

SOURCE: Congressional Budget Office.

NOTES: Caps on discretionary spending are set by law through 1998. Measures of the deficit "with discretionary inflation" assume that discretionary spending grows at the rate of inflation after 1998. Measures of the deficit "without discretionary inflation" assume that discretionary spending remains frozen in dollar terms at the level of the 1998 caps.

n.a. = not applicable.

a. These changes represent only one of a large number of possible paths that would lead to a balanced budget. The exact path depends on when deficit reduction begins and the specific policies adopted by the Congress and the President. The path illustrated in this table is not based on any specific policy assumptions but does assume that policies are fully phased in by 1999.

b. Surplus of less than $500 million.

Chairman ARCHER [presiding]. Bob, thank you very much for, as usual, your very concise and explicit presentation. There are innumerable questions that the members of the committee would like to ask and I just got a question here myself.

Other than population growth, why does Federal spending have to increase at so much more than the rate of inflation? Let me exempt the medical programs from that which seem to follow a course of their own. But if you exempt the medical programs, I believe your testimony was you project an average of 5 percent increase in the rest of the programs and yet inflation is projected at somewhere considerably below that, if I am not correct. Why does government——

Mr. REISCHAUER. About 3 percent.

Chairman ARCHER. Yes. Why does government spending at the Federal level, aside from population increases, have to increase at so much more than the rate of inflation?

Mr. REISCHAUER. I think you have to go at this program by program, and one big program, of course, would be Social Security, and with Social Security you have, as you say, population changes. More people are on Social Security each year. But let's abstract from those changes.

But you have to remember that the new people coming on to Social Security have histories of higher earnings and because they have higher earnings histories, they receive higher benefits than those who are leaving the system because they are dying. So that would be one source of growth.

Chairman ARCHER. Right. Are there any others you can think of? I know that is a big program, but that is still relatively small compared to the rest of all the spending outside of medical programs.

Mr. REISCHAUER. Another big chunk of our spending goes for interest, and interest is driven by interest rates and the size of the Federal debt. As long as the Federal debt grows because we have deficits, it is going to rise at whatever rate you have programmed in for the increase in overall debt.

Chairman ARCHER. Do you project that the interest on the debt will rise more rapidly than inflation as a government expenditure?

Mr. REISCHAUER. Yes, I think it rises as a percent of GDP, so it is rising more rapidly than GDP.

Chairman ARCHER. That I think becomes very important because it relates to the testimony the administration has been giving us in which they insist that we didn't need to worry about the fact that we aren't getting to a balanced budget because we were restraining increases in the deficit relative to GDP. If interest is still going to continue to rise higher than the rate of inflation, it seems to me it is something we do need to be concerned about. I want to ask you this.

Do you think that for the best interest of the country that the deficits projected in the President's budget should be lower?

Mr. REISCHAUER. I think it would be desirable to bring the deficit down substantially over the next 5 years, and the President's budget basically holds the line on the deficit.

Chairman ARCHER. I don't want to put words in your mouth, but would you agree with me that we should be concerned that the debt at the end of 5 years under the President's budget, as they project, it would be $1 trillion more than it is now and as you project it? I suppose it would be a trillion, one hundred-and-some-odd billion more or maybe even more than that.

Mr. REISCHAUER. More than that.

Chairman ARCHER. What would it be under your projections?

Mr. REISCHAUER. I will have somebody find that out.

Let me say that I think we should be most worried about the debt in relationship to the size of the economy, the debt-to-GDP ratio. Under our baseline projections, that debt rises from roughly 52 percent, the ratio rises from 52 up to 53, 54 percent, roughly, under the President's proposal. I think the increase isn't great, but we should be designing our fiscal policy in such a way as to make that ratio decline, as it did steadily from the end of World War II to the beginning of the seventies.

Chairman ARCHER. So if I understand you correctly, under your projections, the deficit grows relative to the GDP?

Mr. REISCHAUER. Yes.

Chairman ARCHER. Under the President's budget.

Mr. REISCHAUER. We have not analyzed the President's budget, his proposal. We will be doing that over the course of the next month.

Chairman ARCHER. Oh, I understand. You were just comparing baseline.

Mr. REISCHAUER. Our baseline to his view of what the baseline is.

Chairman ARCHER. OK. Assuming that their budget estimates are accurate and that they fit with yours when you do examine the impact of their budget, we would have $1 trillion more debt at the end of 5 years, which if the interest rate was 7 percent averaging between long-term and short-term debt, 7 percent would add $70 billion a year of extra debt service obligation. If it is only 6 percent, it would be $60 billion a year of extra debt service charges. The average person in my district is very concerned about that, and I wonder if you have any concern about that also.

Mr. REISCHAUER. I do, as I expressed. I think we should be on a path toward a declining deficit. Our projections under a baseline policy suggest that the net interest costs—these aren't gross—will be $235 billion this year and will grow to $310 billion by the year 2000. So we are talking about a substantial increase, well above inflation in interest costs.

Chairman ARCHER. Let's move off of budget now and on to the estimating process, which is being more talked about all the time. I think you would agree with me that whatever model we use for estimating should be refined and updated regularly to attempt to be as accurate as possible, and that our goal should be accuracy without getting into the argument of dynamic and static. We should always be shooting for accuracy.

In that regard, it is my understanding that under the current budget estimating process, the CBO issues a baseline twice a year and that irrespective of what happens in the interim, that baseline remains constant until the next estimating period. Well, that is a sine qua non.

If you only do it twice a year, it is going to stay the same until the next 6-month period occurs. We could make a massive change in the way we collect taxes 2 months into your 6-month estimating period and there would be no change whatsoever relative to the macroeconomic impact on that in the estimating, as I understand it today. Only at the end of the next 4 months when you once again reestablish your baseline, in hindsight you would then work that into your baseline?

Mr. REISCHAUER. That is true. But I think the real situation is even worse than you have portrayed it, Mr. Chairman, and that is that you adopt a budget resolution by April 15 in theory. That budget resolution is accompanied by a set of economic and technical assumptions.

All of the scorekeeping that is done for the ensuing year is done on the basis of those economic and technical assumptions, even if they appear to be out of date, which is an unfortunate necessity. You have to have some kind of accounting framework in which to judge whether you have complied with the plan that you approved for yourself in the spring of each year.

We will update our forecast, as you say, in August, and if massive policy changes are enacted that would affect the course of the economy, they would be reflected in the economic assumptions that we publish in August, but that would not change the set of economic assumptions underlying the budget resolution.

That is the bad news. The good news is that in theory, if you are going to pass a massive set of policy changes, those policy changes are discussed during the process of formulating the budget resolution. Then when the economic assumptions of the budget resolution are put together, they are not necessarily our numbers. The Budget Committee decides on these assumptions.

They incorporate the assumed policy changes that are going to be passed in the course of the next year. So if you have some massive reform, it would be embodied in that budget resolution and would be reflected in the economic assumptions of the budget resolution. So the totals wouldn't be misestimated.

Chairman ARCHER. I am not sure I follow the latter part of it. I follow the former part.

Mr. REISCHAUER. I am saying that the policy will change the economy but the assumptions that underlie the budget resolution will have assumed that the effect has taken place. So when estimates of the deficit or total revenues or spending are made for the budget year or the following years, they will be accurate in the aggregate.

Chairman ARCHER. Well, I don't want to belabor this, but I think it is very, very important to the entire process by which we operate here. If the assumptions on which we establish a budget resolution are those that predate the policy changes in the budget resolution, it must be because we have a baseline in place.

Mr. REISCHAUER. Let me give you an example. In 1990 when you and others were part of the summit negotiations during our first meetings in the Capitol, I was given a set of instructions: go back to CBO, assuming we are going to do 500 billion dollars' worth of deficit reduction over the next 5 years, and produce an economic forecast, not the one you have given us that assumes a continuation of current policy but an economic forecast that reflects the deficit reduction. We went back and changed our forecast and brought it to you, and that was basically the forecast that was used to underlie all of the estimating for the deficit reduction measure that was cobbled together in October.

Chairman ARCHER. But is that standard operating procedure?

Mr. REISCHAUER. No, it is not standard operating procedure because you don't make 500 billion dollars' worth of policy changes as standard operating procedure. Whenever you have made massive changes, these changes have been reflected in the budget resolution economic assumption. It was done that way in the early eighties when the Reagan policy changes were instituted. But most of the time Congress is really fine-tuning, not making massive changes.

Chairman ARCHER. I understand that. But let's update for today. We are contemplating the possibility of $200 billion in changes which I have some problems with the scoring, but nevertheless that is the way it is scored as a $200 billion revenue loss. So, we are contemplating having spending reductions that will be equal to $200 billion. All of the estimates are overlaid over an existing baseline. Now the net impact on the deficit, if that hypothesis is correct, is zero; $200 billion revenue loss, $200 billion revenue gain.

Mr. REISCHAUER. Right.

Chairman ARCHER. However, the makeup of those items and the impacts on the economy vary differently.

Mr. REISCHAUER. Yes.

Chairman ARCHER. None of that is in any way factored into the baseline assumptions except in hindsight after it occurs.

Mr. REISCHAUER. That may or may not be true. I mean, if you had a particular policy that left the aggregates—the total deficit unchanged but the composition of policy changed radically, as you are suggesting, and we and other economists thought that this would affect the economy over the next 5 years and we were asked to do a forecast, which you would then use for your budget resolution, we would factor that in.

The little pamphlet that the Joint Tax Committee put out about the tax proposals in the contract has two very good pages at the end discussing the possible effects of the contract's proposals on the economy. By and large, I think they concluded that these would be slight over the next 5 years. I mean, if we are looking out over a decade or so, you might reach a different conclusion.

Chairman ARCHER. I would like to explore this further but I will do it privately some day when you and I can sit down and have a cup of coffee.

Mr. REISCHAUER. Be glad to.

Chairman ARCHER. Not having the whole committee sit here.

In your opinion, is the CPI estimated accurately under the current method that is used by the Bureau of Labor Statistics?

Mr. REISCHAUER. We issued a report last fall that said we thought that the current methodology, probably through no fault of the BLS, Bureau of Labor Statistics, overstates the cost of living by between 0.2 of a percentage point and 0.8 of a percentage point. Since we issued that report, the BLS has made one methodological change—or several methodological changes—that should lower that range that we produce to probably 0.1 of a percentage point to 0.7 of a percentage point. There are other aspects of the CPI which probably cause it to be an overstated measure, and the BLS and others are working to isolate these and modify their methodologies.

Chairman ARCHER. Well, whether it is overstated or understated, it seems to me that the same standard should apply and that is one of accuracy, to move toward accuracy because it is a thread that is woven through the fabric of all of our lives in so many different ways.

Mr. REISCHAUER. I think that is right.

Chairman ARCHER. I would be interested as to whether what I have been told is accurate or not. I am told that the basket which is used to develop the CPI, the items that go into the basket, and the interrelationship of those items is adjusted only once every 10 years. It is clear to me the changes that go into this basket and that are interrelated change every year at least. Would you agree with me that we ought to provide the wherewithal, computers or whatever else is necessary, to update this annually rather than every 10 years?

Mr. REISCHAUER. I think doing it annually would probably make it a very difficult and expensive task, but certainly we ought to do it every few years. In this issue we have been penny-wise and pound-foolish over the last few decades. We haven't invested enough in data collection and statistical analysis in our government agencies to save us the money that we should be saving, and I think you are going in exactly the right direction.

Chairman ARCHER. Thank you very much.

Mr. Rangel.

Mr. RANGEL. Mr. Chairman, I enjoyed your exchange with the doctor. I hope you might consider having the members together where we can have an informal exchange like that because it is very helpful and educational.

Doctor, I see that the budget increases the money for drug treatment from 13.3 to 14.6 and it is abundantly clear to me that the administration, like those before it, haven't the slightest idea as to what is happening with that money. Having said that, has your office ever prepared any paper to suggest what economic impact this drug situation is having on our overall economic situation, that is, the loss of moneys for law enforcement and drug treatment?

Mr. REISCHAUER. No, we haven't. We have had some discussions with your staff in an attempt to isolate sources of information and data that might shed some light on that question. I think it is a very complicated question, a very serious and important one.

Mr. RANGEL. Well, everyone seems to agree that as we move forward in international trade and see the gap widening between the skills that are available and those that are going to be needed, that drugs impact on the education we receive and the number of people that are able to be in the work market. From an economist's point of view, I just don't see how that doesn't factor into everything that we talk about.

Whether you are talking about trade or health or crime or productivity, it just never seems to come up. It is as though this is something we shouldn't talk about. It is not in the State of the Union. It is not in any of the statements of Cabinet officials. Maybe the question should be how important is it to the type of work that you do when you present to us an overview of the budget and you can't see your way clear to mention the drug epidemic, which worsens every year.

Is it really not important enough to be mentioned? Or is it the other similar type situations that we just accept and would not normally expect that would be included in a report such as this that you give?

Mr. REISCHAUER. I share your concern for this problem and I think it is an important one. But it is one about which there is very little information that could be used to estimate the impact on the economy. We know that the U.S. economy is not as productive as it might be if the country's drug problem—substance abuse broadly speaking—were not so serious.

If anything would affect our forecasts, it would be the reflection that the problem was worsening or getting better in a significant way. Otherwise, it is in a sense built into the base set of numbers, the base set of relationships that we use to forecast where the economy is going.

Mr. RANGEL. Well, I don't know whether it would be just a blip on the screen, but if we started in 1960 and you project that the drug problem would be going up, interest rates would go up and the impact this would have on the budget, our revenues, our productivity, I mean to me it is a national crisis, but I am just trying to figure what type of a similar situation that would have a similar impact on your forecast would you include. I mean, you can't project epidemics.

You can't project disasters in certain parts of our country that causes hundreds of billions of dollars' worth of damage. But it just seems to me that when you have an epidemic of this size that impacts on everything that we do, that somehow it would be mentioned, if not by you then by somebody. It is not even in the State of the Union Message.

It could very well be that it is not that important, that it is just something we have to live with. We don't talk about AIDS, either. If that is the way economists look at it, then I will just have to change my way in what I expect from a government and from the offices that monitor what we do. I don't mean to be critical of you.

Mr. REISCHAUER. No, I know.

Mr. RANGEL. It may be outside of your scope, but I don't know where to go.

Mr. REISCHAUER. I think the appropriate place to go is to the executive branch on these types of questions, because they have a responsibility and a set of programs that are designed to deal with this problem.

Mr. RANGEL. That wasn't really my question and my time has expired. My question was as relates to your forecast and the economy whether or not the drug problem and the impact on the things that you suggest may or may not happen as you see it and whether dramatic changes in that would change your reports to us in any way.

Mr. REISCHAUER. If we saw dramatic changes about to occur as part of baseline policy, I think it would affect how we looked at the economy, the costs of certain kinds of programs. But as we look into the future, we don't see that kind of dramatic change built into current policy.

Mr. RANGEL. You mean this thing about addiction going up from 1950, the way it is going up, that if you had known it was going to do that that it would not have changed your forecast?

Mr. REISCHAUER. We didn't begin forecasting until 1975, so we came in half way up the slope that you are talking about. If we had had perfect foresight, we might have expected productivity to grow less rapidly.

Mr. RANGEL. Thank you.

Mr. THOMAS [presiding]. The gentleman's time has expired.

The chair recognizes the gentleman from California, Mr. Thomas. Thank the chair. We have to learn how to do these things.

For the record, I really want to thank you and your shop. For folks who are not in the middle of the requirements placed on you and your people during the 103d marathon on health care reform, in which we labored long and we got nothing except knowledge about how to do it, that work is going to pay off in the long run. We had never really done that kind of macro stuff that quickly in as many ways before, I believe. But most people do not realize the time constraints, the pressure constraints, the stress constraints. You folks did a marvelous job, and I just want to give you as much credit as I can and I will be doing so in the future. I want to thank you for the effort you folks carried out.

Mr. REISCHAUER. Thank you.

Mr. THOMAS. The gentleman from New York in his early initial comments mentioned getting together and talking about some of these things I think are absolutely essential. Wherever you go, I want to make sure that we try to have these conversations. He made one point and, given his background, his knowledge and concern, he is focusing on the drug problem and the enormous negative drag on the economy that it is, that it would be a mistake not to talk about human suffering and the wasted human opportunity, potential from an economic point of view.

My problem is, I am now sitting here looking, for example, in my narrow subcommittee responsibilities, at the health insurance fund on Medicare part A. We have already lifted the total income cap, we are at 1.45 and you are sitting here looking at what you have got to do to avoid bankruptcy by 2001.

You say, gee, let's double the tax and then you look at how meager the results are in terms of having bought some time. You realize you have to probably triple it and then take a look at what you do to the employment rate and the economy to do that, or you have got to cut benefits by two-thirds to live with the old structure. We talk about the underground economy. Just this morning IRS is leaving $5 billion on the table because they simply haven't been matching up Social Security numbers with people, and it is a great new advancement in terms of what we are doing.

The CPI index is not accurate and even if you get it accurate for one group, it is significantly different for another. You begin looking at all of these things that we have got to do and the thing that comes to mind initially to me is that when I first came back here and they told me let's go eat some Chesapeake crabs, I went out and I started doing that. I looked at all of this labor that I was putting in to get this very minuscule amount of crab meat and they said have a cracker. I said well, I want to eat the crab meat. I began to realize if you don't eat crackers periodically, there is a net deficit in terms of nourishment versus labor on this.

Mr. REISCHAUER. That is why Ms. Johnson and I, coming from New England, would argue that you should eat lobster.

Mr. THOMAS. There is the point. What we have been doing recently is kind of Chesapeake Bay crab eating on playing with how we adjust this stuff. I look at your numbers in terms of holding the discretionary inflation rate to zero, a drop in the bucket with enormous pain and the rest. Don't we need to rethink the way this Federal Government gets the resources necessary to do its job? Couldn't we, if we focus on the way in which we raise the revenue fundamentally, rethink it so that we can accomplish more than all of the little adjusting that we intended to have gotten into?

Or is that a fallacy and it is not an easy way out, the idea of a flat tax or pure consumption tax or some other kind of a change in relationship between getting revenue and spending it?

Mr. REISCHAUER. I didn't expect that question to end where it did, because I thought you were going to talk about fundamentally restructuring the spending side of our budget.

Mr. THOMAS. Why don't you do that after you tell me there is no way you can really do it on the revenue side?

Mr. REISCHAUER. I was going to tell you that on the revenue side, revenues under the current structure are growing at about the same rate as the economy as a whole. There might be dead weight losses and costs that could be reduced by changing the nature of our tax system, but there are other changes that——

Mr. THOMAS. Would that hit some of the underground economy, all of these suggestions about tapping sources that are not tapped in the system or counting trends that are not now in the system? Isn't that marginalized and working on the margin?

Mr. REISCHAUER. I think it is. I think even the large-scale adjustments that you are talking about, substituting consumption tax for tax on labor, income, or whatever would not resolve the problem that we are talking about. I think there is a desire among people to keep taxes about constant as a percent of income. If that is the case, you have to look at the spending side and say what can we do to make sure that spending rises no faster than gross national product or the income of the Nation?

Mr. THOMAS. So despite some of the politics going on now and perhaps the imperfectness of the recent Republican or majority approach, that if we are going to get the fundamentals in balance, I guess I am asking you, we really do have to address the spending.

Mr. REISCHAUER. You must not just address spending, but of course the extremely rapid growth on the spending side is concentrated in the medical programs.

Mr. THOMAS. One of my major disappointments is that this is the last year the President really has control of his budget and he had been bold, as I said yesterday, flawed but bold, in his plan last year with a $124 billion reduction in Medicare over 5 years. But he doesn't really offer anything this year except a receptiveness to work together.

That scares me because in a receptiveness to work together without a plan, we are going to be driving it and we are going to be coming up with a plan but we lose another year. Folks just aren't focused on the fact that 2001, 2002 are not just the balanced budget years we are talking about. It is the bottom dropping out, bankrupt years on programs that are going to take years of adjustment to make in terms of denying people benefits they think they are going to get now.

If you don't start now, you can't get to where you need to go on a glide slope that will be acceptable to people. I am looking forward. We will find out where you are and what you are doing. Just some short-term guidelines.

For example, a very interesting discussion with Chairman Archer. Do we compound some of the problems you were talking about by going to a 2-year budget cycle or are there internal adjustments going to a 2-year budget cycle that will not exacerbate the problems that we have in a 1-year budget cycle that you had discussed?

Mr. REISCHAUER. I have never been a fan of a 2-year budget cycle. When we are as far out of equilibrium as we are right now, I think these issues should be on the table every year because some years the economy won't be right or the politics won't be right. I think that cutting in half the number of years in which you have an opportunity to raise fundamental issues would be a mistake.

If we were operating with a balanced budget, that might be fine. But that isn't where we are right now. We are trying to grab whatever opportunity we have to make changes, and I think reconsidering everything every year is the appropriate schedule.

Mr. THOMAS. Thank you very much, Dr. Reischauer.

Once again I really do want to thank you folks for an effort that was just extraordinary over an extraordinarily long period of time. We can all gear up for something if we think it is going to be 2 weeks or 1 month. I don't think any of us thought it was going to last as long as it did.

Thank you very much, and the American people will eventually understand what a contribution you and your folks made.

The gentleman from Nebraska, Mr. Christensen, may inquire.

Mr. CHRISTENSEN. Thank you, Mr. Chairman, and thank you, Dr. Reischauer, for coming. I do appreciate your testimony and your work here. I wanted to briefly visit with you about the President's budget, as well as some things about CBO.

But I wanted to first bring your attention to what is happening in middle America concerning the President's budget. This was yesterday's lead editorial in the Omaha World Herald. It said, "Clinton's poor excuse for a budget makes deficit cutting claim a joke." This is a paper that is not overly conservative. They didn't endorse me in the campaign. They have given a lot of credit to what has gone on here recently.

This was today's editorial. "White House budget abdication passes the buck to Capitol Hill."

So the Omaha World Herald has some pretty good editorials. As far as I am concerned, the President's budget didn't go nearly far enough.

My concern is that we are going to rack up $1 trillion of debt with the President's budget over the next 5 years. You talked a little bit about CPI, and Senator Kerrey this week talked about reexamining the CPI to see if it remains accurate, especially given the great impact it has on the cost of Medicare, Medicaid, and pensions for the military.

Could you share with us your thoughts, and rationale behind those thoughts, as well as if that is something we should do?

Mr. REISCHAUER. As I said before, we have done a study that suggests that the CPI has some bias in it, and is an overestimate of the change in the cost of living.

Mr. CHRISTENSEN. If it does have some bias in it, do you have any estimate on how many billions of dollars that might be costing us if it is off a little bit?

Mr. REISCHAUER. Yes, I do, and I will mention that in 1 minute.

As I said in answer to the chairman's question, right now our best judgment would be that the overestimate is somewhere between one-tenth of a percentage point and seven-tenths of a percentage point per year. That is a considerably lower range than was provided by the Chairman of the Federal Reserve.

As I said, this is not of a new discovery. Economists and the people at BLS have known about this for a long time. A lot of effort has been put into trying to improve the CPI, and it is continually being improved, but it takes a lot of resources which the Bureau of Labor Statistics hasn't had, to make these improvements, and they take time.

If the CPI were overestimated by half a percent and you lopped it off by half a percentage point over the next 5 years—through the year 2000—that would reduce the deficit by $64 billion.

Of that $64 billion, $6 billion would be debt service. Because we have lower deficits, we would have lower interest payments.

Of the $64 billion, $22 billion would be higher revenues, because we use the CPI to index the parameters of the tax system every year. The $26 billion would be from the Social Security system.

So it is largely Social Security and revenues that would account for three-quarters of the adjustment here.

Mr. CHRISTENSEN. Do you have any estimation or any idea for the new CBO Director to follow and the administration if they look at it as if it is going to be a long process? We are talking about just under one-third of that—you said about $64 billion?

Mr. REISCHAUER. Over a 5-year period. In the last year, the year 2000, it would be about $25 billion.

Mr. CHRISTENSEN. That would be a significant——

Mr. REISCHAUER. That is real money, yes.

Mr. CHRISTENSEN. It would be nice to see the CBO move in that direction if the figures back that up.

Mr. REISCHAUER. There are two directions in which you can go. One is that you can provide BLS with a lot more money, a lot more resource, and some direction to proceed as fast as it can to make whatever improvements can be made.

But these will occur gradually over a decade-long period. There is no question about that at all. You might never be able to isolate and correct some of the misestimations. That is one direction.

The other is to say that academicians and economists have told us that a misestimation exists. We are therefore going to change Social Security law, the Internal Revenue Code, and so forth, to make indexing the CPI minus three-tenths of a percentage point, or four-tenths of a percentage point, or something like that.

Those are the two directions. The latter direction is more sure, and it would be scored by the Congressional Budget Office and the budget process. You would get credit for it. But you would also get the other side of that coin, which is objections by all of those people who will be paying higher taxes or receiving less in the way of index benefits.

Mr. THOMAS. The time of the gentleman has expired.

Mr. CHRISTENSEN. Thank you, Dr. Reischauer.

Thank you, Mr. Chairman.

Mr. THOMAS. In addition to the political problem of giving somebody something minus something, if you readjust the CPI, you are giving them the new CPI instead of minus, from the political point of view.

Mr. Ensign.

Mr. ENSIGN. Thank you, Mr. Chairman.

Dr. Reischauer, there has been a lot of talk about dynamic and static scoring. I know that Mr. Christensen has talked about some uses already in place of dynamic scoring in the budget process. In your opinion, do we use any dynamic scoring right now?

Mr. REISCHAUER. We take into account behavioral responses. So the estimates that are done now, both on the outlay side and on the revenue side, are in no way static estimates. They assume that when gasoline taxes rise, people buy less gasoline. I should say that the Congressional Budget Office does not provide revenue estimates. They are done by the Joint Committee on Taxation.

The issue that has really been debated is whether changes in policy could have macroeconomic implications; could they change labor supply, saving, and investment, in such a way that economic growth might be increased or decreased as a result of the policy?

Those types of effects have not been built into the estimating process for a number of reasons, one of which is that there is a good deal of debate in the economics community about the size, magnitude, timing, and even the direction of these kinds of effects.

Some economists will say that this will strengthen the economy, and others will say that this will weaken it. It is not clear that you want the estimators to have a lot of latitude in which they could come up with numbers that were plus or minus. The numbers would then be subject to a lot of criticism.

These effects are really very small over the 5-year period that we are providing estimates for, and it is important to realize that if you were going to move in this direction, you would want to do it in an evenhanded manner. You would want to deal with spending as well as revenues. There are various spending programs that arguably could slow down or energize the economy.

It is a very complicated issue.

Mr. ENSIGN. Right. I agree with Chairman Archer, whether there are or aren't, I think what we need to be looking for, as much as we can, is accuracy. Before my term here I was just obviously a normal, average, everyday businessperson and citizen, hearing not only a lot of criticism of estimates from CBO, but from practically anybody else who does estimating.

Has CBO analyzed itself or has an outside agency analyzed CBO to measure how accurate you are on a year-to-year basis, on a 5-year basis? How close do you come to your projections over time?

Mr. REISCHAUER. We publish, as an appendix in one of our annual volumes, an analysis of our economic forecasts and how well they have done in comparison with the Blue Chip Consensus and the administration's forecasts.

Mr. ENSIGN. How about relative to what happened?

Mr. REISCHAUER. That is what I mean. We compare all three to what happened. I mean not CBO versus the profession, but CBO versus the other alternatives you have versus what actually occurred.

Mr. ENSIGN. OK.

Mr. REISCHAUER. We also include in each of our updates an analysis of the change in our budget numbers, outlays, and revenues; how much of the change that we are projecting now is attributable to changes in economics; how much in turn is attributable to changes in policy; and how much is attributable to technical and other factors, which include errors on our part.

We also include an appendix in these volumes that compares our budget estimates with the administration's budget estimates versus what actually happened. So we have been pretty straightforward and laid this information out for a long period of time.

Mr. ENSIGN. But how accurate are you?

Mr. REISCHAUER. You want to know how accurate we are? We are not very good but we are better than the alternatives.

Mr. ENSIGN. I would like a number. Are you within 10 percent? Are you within 5 percent? 50 percent? Overall, on average, what would you say your error margins were? When you give us a number, is it within plus or minus 2 percent, plus or minus 10 percent?

Mr. REISCHAUER. Below 10 percent for sure. These are done in absolute dollar terms, and the economic differences are done with absolute values. To really examine these, you'd need to look at various statistical measures.

Mr. ENSIGN. If you get into standard deviations, you are going to lose me. Thank you.

Mr. REISCHAUER. Then I will start.

Mrs. JOHNSON. Thank you, Mr. Ensign.

Mr. Coyne will inquire.

Mr. COYNE. Thank you, Madam Chairman.

Director, over the last month or so we have heard an awful lot of testimony from economists, executives, Governors, mayors, a lot of people, and all too often it seems to me that when they refer to the unemployment rate, they consider 5.6 percent as being full employment.

Is that where we are at in this country today that with 12 or 14 or 15 million people unemployed, we are at full employment?

Mr. REISCHAUER. I would rather not use the term "full employment," because that makes it sound like everybody who wants a job can have a job, and that is certainly not the case.

We refer to it as the natural rate or the nonaccelerating inflation rate of unemployment, which simply says that when the unemployment rate is lower than it is now, inflationary pressures will build. That is a very neutral statement with respect to whether everybody has a job who wants a job or should have a job. It is not saying anything about that. It is saying that if you push the unemployment rate down much below 6 percent, inflationary pressures are going to build.

There will certainly be people looking for jobs, but there may be a mismatch of skills in relation to the jobs that are available.

Mr. COYNE. Is that to say, then, we ought not to do anything to get the economy moving to take care of the others?

Mr. REISCHAUER. Economists feel that if you adopted fiscal policies that would stimulate the economy, in other words, increase total demand by tax cuts or spending increases, the Federal Reserve, which is responsible for trying to maintain a steady rate of inflation at a low level, would tighten monetary policy and offset any of the expansionary impact that your fiscal policy steps might have taken.

Mr. COYNE. From your reviews, is there any evidence that most of those 12, 14, 15 million unemployed people are just people in transition from job to job?

Mr. REISCHAUER. First of all, it is not as many people as you are suggesting. The unemployment rate right now is 5.7 percent, and the labor force is roughly 125 million people. So we are talking about 8 or 9 million people.

That group is made up of some people who are entering the labor force and are looking for a job; some who have voluntarily quit jobs and are looking for a new job; and some who have been laid off or lost jobs involuntarily and would like to find another.

Mr. COYNE. But it does not include the discouraged workers?

Mr. REISCHAUER. No, it doesn't. The 5.7 percent doesn't, although there is an additional measure that does include them. We count them on, I believe, a quarterly basis, so we have some idea of how many discouraged workers there are, as well.

Mr. COYNE. You were asked about the accuracy of the CPI index, and whether that is really being estimated in the most accurate way that it can. How do you feel about the way the Department of Labor makes its estimates about unemployment? Are we doing the best job we can there?

Mr. REISCHAUER. They have tried to improve and expand that survey, and major changes were made in it 1 year ago, in January. We used a new survey instrument that attempted to find some of the people who were thought to be unemployed who were not being recorded, and the feeling was that the unemployment rate jumped several tenths of a percentage point as a result of this improved survey instrument. I think they are continually doing that, and also doing special studies to find answers to the kinds of questions you have been asking, about discouraged workers and the composition of the unemployed.

Actually, the total number of unemployed last month was about 7.5 million people.

Mr. COYNE. Thank you very much.

Mrs. JOHNSON. Thank you.

Thank you, Mr. Coyne. Mr. Reischauer, I was pleased you included in your testimony a section on the illustrative path of the balanced budget. I want to take my time to see that I understand it correctly.

I am sorry I missed the actual presentation of your testimony, but I have read some of it now and will read it all. I welcome you back and admire your work and look forward to working with you in this very difficult time.

But through a period when I think we do have a chance to address some of the problems that we have not addressed in recent years.

My understanding of this section is that in order to reach a balanced budget by the year 2002, we have to cut $322 billion, effectively, that year.

Mr. REISCHAUER. That year, you would, if you followed the path that we laid out; if you followed some other path, you might have to cut more.

Mrs. JOHNSON. Let me see if I get the outlines of that path correctly. You say if we freeze discretionary spending at the 1998 level——

Mr. REISCHAUER. In nominal terms.

Mrs. JOHNSON. Which you point out is a 22-percent real cut by the year 2002.

Mr. REISCHAUER. In current 1995 appropriations levels, right.

Mrs. JOHNSON. Which is substantial. We are talking quite a few years out, now. But if we freeze discretionary spending, then my understanding of your testimony is that of $322 billion, we save $89 billion. Am I relating the right numbers here?

Mr. REISCHAUER. Yes. That includes the savings from freezing discretionary spending, plus the debt service associated with it.

Mrs. JOHNSON. Right. Then later on you mention that if by the year 2000 the market is convinced that we are committed, that you would anticipate there could be a drop of as much as 1 percent in interest rates which would by the year 2002 save $140 billion.

Now, is it correct to interpret your testimony that if we add together the $140 billion and the $89 billion, that is $229 billion of the $834 billion? So what we are looking at is the policy changes that would accomplish the other $93 billion?

Mr. REISCHAUER. Yes. You would subtract. In that table there is a total of 1.035 trillion dollars' worth of policy changes.

Mrs. JOHNSON. How many?

Mr. REISCHAUER. Over this whole period, $1.035 trillion. You can subtract from that the savings that you would get from discretionary spending, which would be $212 billion, up in the right hand top corner. This is over the 5-year period.

You were mixing a single year's number with a 5-year number, and just now I was translating everything into 5-year terms. Would you like to stay on just the year 2000?

Mrs. JOHNSON. I am trying stay on the year 2000 and look at what besides freezing at the 1998 level plus the interest rate benefit that you expect to get? What are the dimensions of the remainder?

Mr. REISCHAUER. OK. You can add to the $89 billion roughly $38 billion in additional interest savings. In other words——

Mrs. JOHNSON. So you can't add the $140 billion?

Mr. REISCHAUER. No. The $140 billion is summed over 5 years.

Mrs. JOHNSON. Do you go on elsewhere and enumerate——

Mr. REISCHAUER. This really means that in that table, rather than having to take $180 billion from policy changes in the mandatory or entitlement area, you would only have to take about $142 billion.

Mrs. JOHNSON. Your policy options here are, if you freeze discretionary at the 1998 level, which means taking a 20-percent reduction in real costs from the 1995 level, then the remainder of the problem is basically 140 billion dollars' worth of policy changes in the entitlement area or tax areas.

So the defense cut would be the freeze?

Mr. REISCHAUER. The defense——

Mrs. JOHNSON. The impact of the defense budget——

Mr. REISCHAUER. Would be part of the freeze, yes.

Mrs. JOHNSON. So the remainder of the $140 billion is entitlement plus any revenue freezes?

Mr. REISCHAUER. Yes.

Mrs. JOHNSON. If you were to take that all in entitlements, have you looked at what would be your policy options, including also tax entitlements, tax expenditures?

Mr. REISCHAUER. No, we haven't gone beyond this total level to propose policy changes. We present to the Congress a large options book each year of various ways to reduce the deficit by cutting spending on both discretionary and entitlement programs and raising taxes.

Can you go through that volume and make up a particular package?

Mrs. JOHNSON. Thank you very much.

The gentleman from—Mr. Portman will inquire.

Mr. PORTMAN. I thank the Chair, and I thank you for being here, Dr. Reischauer. I have a few questions to relate really to the general issue of how serious is our debt and deficit problem.

I wanted to get your sense of, first, with regard to the issue I raised with Mr. Archer of the ratio of our debt to the GDP. In your testimony over the last few days from CBO and Treasury, we have talked about the fact that the President's budget decreases the deficit as a percentage of our GDP and supporters of that budget have said that is a significant measure.

Later in this afternoon's testimony, we asked Dr. Rivlin about the percentage as it relates to debt. I just wonder two things.

No. 1, do you think that the debt as a percentage of GDP is a significant economic indicator? As I assume you would agree, the deficit figure is.

No. 2, in your analysis, and I realize yours is not the President's analysis, although it is actually somewhat close because theirs is a more or less static budget, do you have any sense of what the debt as a percentage of GDP would be over the next 5 years? Would it decrease or would it increase?

Mr. REISCHAUER. First of all, I think that the debt-to-GDP ratio is a very important indicator. We came out of World War II with a debt-to-GDP ratio of about 120 percent. That fell steadily to about 25 percent in the early seventies. It didn't fall because we were running surpluses most of those years. It fell because we were adding to our debt at a slower rate than the economy was growing.

So, a falling ratio is compatible with continued deficits. During the seventies, that debt-to-GDP ratio bounced around in the 25-percent to 27-percent range.

Then it began zooming up. It is now 52 percent. In other words, we have doubled it in the last decade and a half. If we do not change our budget policies, it is going to continue to creep up over the next 5 years.

I think the administration's budget proposal, if it does what it says it is going to do—and CBO has evaluated it yet—appears to stabilize that ratio. It doesn't start bringing it down, it doesn't bring us back into the world we lived in for 20 or 30 years after World War II.

Mr. PORTMAN. From what you understand, you would do your analysis to take a look——

Mr. REISCHAUER. We will evaluate the President's budget and provide estimates for what we think will happen to that debt-to-GDP ratio under his policies.

Mr. PORTMAN. That would be very interesting, I am sure, to a lot of us. Second, and this is a very general question, if you could give us your normally succinct answer, and this is to focus on the importance of this issue, what is wrong with the deficit spending we are doing, and having $200 billion deficits as far as the eye can see? What impact does that have on the economy?

We have heard about 16 cents on $1 going for interest on the debt. We have heard about unavailable capital. What is the problem with it?

Mr. REISCHAUER. The problem is that we are a nation that doesn't save very much. We don't save much as individuals or as businesses. When the public sector runs a deficit, it absorbs some of that saving to use for goods and services that the government is providing.

Less saving is therefore available for private productive investment, from which comes economic growth. To some extent that lack of available saving can be made up by an inflow of foreign money, but then you are dependent on capital flows into your country to sustain economic growth.

If the government were using the resources that it was absorbing from the private capital markets to invest, to expand in, let's say, government programs that arguably might strengthen the economy over the long run—education, training, research and development, certain kinds of infrastructure that have been shown to make the private sector economy more productive—then you wouldn't be tremendously worried about this deficit.

But that is not what has happened over the last 20 years. The growth of the deficit has been accompanied, not by an expansion of investment-oriented spending that the government does, but rather by consumption-oriented spending.

We are basically reducing the expansion of the capital stock of our country; therefore, future living standards and wages won't be as high as they would otherwise be. It is not that they will be lower than they are now, given current policies. It is just that they won't grow as rapidly as would otherwise be the case.

Mr. PORTMAN. Thank you. Mr. Chairman, I want to thank the Director for his help on the unfunded mandate front. Tell him that I apologize for adding to his already burdensome task, but I appreciate the support.

Mr. REISCHAUER. I am going to escape this task.

Mr. PORTMAN. Is it because of unfunded mandates that you are leaving?

Thank you, Mr. Chairman.

Mr. REISCHAUER. My staff, by the way, appreciated very much the work that they did with your staff. They found your people very good.

Mr. MCCRERY [presiding]. Thank you, Mr. Portman.

Mr. Payne.

Mr. PAYNE. Thank you very much, Mr. Chairman. I want to associate myself with Mr. Thomas' remarks and commend you and your staff for the work that you did in 1994, certainly in health care reform, as well as in OBRA 1993, OBRA 1990, and other important bills.

Mr. REISCHAUER. A lot of sleepless nights.

Mr. PAYNE. A lot of sleepless nights. I do think that Congress is becoming increasingly responsible as it relates to matters of fiscal policy. I certainly think you and others at CBO are an important part of making that happen.

Thank you for that.

Mr. REISCHAUER. Thank you.

Mr. PAYNE. I am one of those who signed onto the balanced budget amendment, maybe out of frustration, but feeling that we had to find a way to get our deficits down and do it at a time certain. I am concerned about the President's budget.

I am feeling more concerned because I see you have even higher deficit numbers in the year 2000 than the President's budget, and I understand that is because of some differences in assumptions about growth and differences in terms of the health care growth rates as opposed to what HCFA has done.

As it relates to what we have been doing on this committee, we have been talking a lot about the Contract With America, much of which I agree with, and much of which is very popular in my district. I am concerned that we on this committee may be put in a position where we have to make a decision about substantial tax cuts without knowing how they are going to be paid for.

If you would perhaps comment on your thoughts about the advisability of these tax cuts being approved before there are specific funding sources, I would appreciate it.

Mr. REISCHAUER. You established in 1990 and reaffirmed in 1993 a set of procedures that in fact should not allow you to adopt tax cuts that are not paid for. If you do adopt tax cuts that are not paid for, under existing law the administration will be required to impose sequestrations, that is, across-the-board cuts on Medicare, farm price supports, student loans, a number of entitlement programs that many might think should not be subject to arbitrary, last-minute cuts.

So I think that if you just stick with the rules that you have established for yourself, fiscal responsibility should reign.

Mr. PAYNE. As I understand it, that is exactly what we intend to do——

Mr. REISCHAUER. That, by the way, is the law of the land. So in a way it doesn't depend on whether you are fiscally responsible or not. The administration is required to take steps if you present them with unpaid-for tax cuts.

Mr. PAYNE. I think the process is for this committee, which typically or generally has been very conscientious in terms of making sure that it pays for its tax cuts——

Mr. REISCHAUER. Very.

Mr. PAYNE. That instead of us acting at this committee level, we will act and cut taxes and send those along and expect them to be joined up with some spending cuts that would happen in other areas at a later time, as I understand it.

Do you have any advice or thoughts about that particular procedure? I, as one member, have concerns about voting, not knowing exactly what it is that would be done to offset the cost.

Mr. REISCHAUER. But remember that this committee has jurisdiction over a very substantial portion of the entitlements spending package. You can't expect committees that have very small amounts of entitlements to cough up the money to pay for a large tax cut offered by this committee.

So this committee is going to have to do some heavy lifting on its own, although, as you suggest, the Agriculture Committee, the Veterans Committee, Energy and Commerce, other committees with entitlement jurisdiction might have to bear or will be asked to bear some of the burden.

But I would urge you to be very, very cautious. The Congress over the last 4 years has been extremely responsible in adhering to the rules and limitations that it created for itself. It would be a shame to go off the wagon at this point.

Mr. PAYNE. Mr. Chairman, could I ask one other question?

Mr. MCCRERY. Be my guest.

Mr. PAYNE. Thank you.

Dr. Reischauer, I guess this question goes to the whole notion of tax cuts in general. As a matter of public policy, we have stated we are trying to get to a deficit of zero by the year 2002, which CBO said will cost $1.2 trillion. The Treasury has said if we pass all the tax cuts that are in the Contract With America, it will add an additional $400 billion, so then it becomes a $1.6 trillion exercise.

Considering the magnitude of those numbers, would you comment on the advisability of tax cuts given those conflicting objectives. Also, given this kind of economy, where we have full employment, should we be doing something that might be stimulative?

Mr. REISCHAUER. Well, you used precisely the right word. Reducing tax burdens and reducing the deficit are both desirable objectives, but they are in conflict. When you do some of one, it makes doing the other harder. The Congress has to decide which it gives higher priority to. It has to ask the American people which they are most interested in, and I think pursue that one so that you achieve the goal. Then you must ask yourself, can you go further to achieve the other goal?

But every dollar that you provide in tax relief is going to require a spending cut just to keep the deficit from increasing. In other words, you are just treading water. If you also decide you are going to balance the budget, it means the spending cuts that you are going to make to bring the deficit down once you have brought it level again will be that much harder.

Mr. PAYNE. Thank you very much.

Thank you, Mr. Chairman.

Mr. MCCRERY. Thank you, Mr. Payne. I can assure the gentleman from Virginia that over the next 2 years he is going to have plenty of opportunity to vote for spending cuts that will more than outweigh the taxing increase that this committee will vote for. So don't worry, we are going to be able to cut spending a heck of a lot more than——

Mr. PAYNE. I am not worried. I would just feel better if I did the spending cuts first, as we have always discussed we felt was the best way to proceed, and then have the tax cuts second.

Mr. MCCRERY. I will assure the gentleman again that he is going to have an opportunity to vote on a package that will include as many spending cuts as we have tax reductions, at the same time.

Mr. PAYNE. In this committee?

Mr. MCCRERY. No, sir, not in this committee. I don't think that is necessary, nor desirable. But on the floor of the House where it counts, you will have an opportunity.

Dr. Reischauer, in responding to Mr. Portman's inquiry on why it is bad to continue having $200 billion deficits, I appreciated your answer, but it is my impression, and I want you to comment on this and tell me if I am wrong and explain why. It is my impression that it is not only bad for the reasons you stated, but also, if you look beyond the 5-year window, or even the 10-year window that we often look down or look through, there are some events likely to occur, absent congressional action, that compound the problem, such as the Medicare Hospital Insurance Trust Fund going dry around the year 2001 or so.

That is more of a relative problem than it is an absolute problem, because we will have to take resources from education, training, research and development, whatnot, and supplement that fund in order to pay the bills. That is a relative problem.

But then further down the road, 2016, 2017, we will face an even bigger problem when the baby boom generation retires and starts calling on the Social Security trust fund and we are no longer able to use the surplus, so to speak, for education, training, and all these other things we would like to do.

To me that says that we need to start taking very serious actions today, this year, to account for those problems that are down the road. Do you agree with that? Am I off base on this? Can you expound on it?

Mr. REISCHAUER. No, I think you are right on the money. We have a short-run problem, namely, that we are running deficits and we would like to have a balanced budget.

The demographic situation in this country means that starting in the second decade of the next century, our programs devoted to the elderly—and those are Medicare, Social Security, and some of the other programs, too—are going to explode. Their spending is going to rise as the numbers of beneficiaries increases.

We as a society, as a nation, are going to have to redirect resources one way or another to provide the retired population with the income they need to live and the income that we have promised them.

There are two things we can do about that now. One is that we can begin scaling back our commitments to future retirees by changing the retirement age, and making other modifications in the Social Security system or the Medicare systems.

The other is that we can strengthen the economy, run surpluses, or lower our deficits so that the total wealth of our economy expands, and there are more resources to channel in the direction of the growing retired population. We probably should be doing both.

Mr. McCRERY. Thank you. Again, it seems to me that with those problems looming out there, we ought to be thinking in terms longer than 5 years or even 10 years. We ought to be thinking of the problems that are further down the road, and how if we don't start doing some things now to prepare for those problems and prepare to be able to cope with those problems better than we would be if we stayed on the present course, we are going to have a heck of a time. We are going to be even more dependent on foreign capital to finance our standard of living in this country.

Won't that put us somewhat at the mercy of the rest of the world if we get to that point?

Mr. REISCHAUER. The rest of the world is going to be in the same shape that we are in. So I wouldn't count on them coming to our rescue. I think the point you made is worth reemphasizing, and that is that you can take modest steps now that will improve things 20 years from now, and will preclude the possibility that you might have to take radical, drastic, and inequitable steps in 2015 or 2020. So there is good reason to act now, even though the crisis isn't looming right in front of us.

Mr. McCRERY. Well, thank you very much for your responses to our inquiries and your testimony of today and for your service to the country and to the Congress. My view is, and it is only my view, that this Congress is going to take some bold steps, or attempt to take some bold steps to address those long-term problems.

It is not going to be particularly popular, I predict. Although I know how the game works, I am disappointed that the President did not come forward in his budget with suggestions for some bold steps so that we could do this in tandem. I am hopeful, I am still hopeful that the administration will accept our proposals, which will come, despite the cynicism of the few. We are going to come forward with some proposals.

They may not be the exact proposals that you would like to see or the President would like to see. But I am convinced that this Congress or a majority of this Congress is very serious about cutting spending for the short term and for the long term to get us to a balanced budget and perhaps even run a surplus so that we will be better prepared to meet those problems when they arise in the next century.

Now I am informed Mr. Houghton would also like to inquire.

Mr. HOUGHTON. I was not going to ask a question, but I can't resist. Mr. Reischauer, great to see you here.

You may not want to answer this, but I am going to ask it anyway. The problem that we are facing is we are putting so much off the table, we put Social Security off the table, we put our interest off the table, we put virtually Medicare off the table, we are putting the military off the table, everything like that.

I mean, the big items, the big money items, we are not really wrestling with, although that may not be so with Medicare and

Medicaid programs. How would you go about wrestling with those things so that we do the steps that are moving toward the solution in 2010, 2015, 2020, rather than moving away from it? What are those specific actions or the areas that you would be working toward in those big money items?

Mr. REISCHAUER. I think I benefit from not really understanding your question, so I have a hard time answering it. I have always been a believer that everything should be on the table, and that people who want to take things off the table maybe ought to be forced to come up with substitutes.

You could pass a bill that cut everything by a flat percent—Social Security, you name it—absolutely everything. Then, if you want to take Social Security off the table, here is a proposal that cuts something else or raises a tax to allow you to take it off the table.

In other words, impose a price on those who want to take some large spending item off the table. That is, to find their proportionate share of the savings to do that.

Mr. HOUGHTON. Well, in other words, you are saying that it may be easier——

Mr. REISCHAUER. I think——

Mr. HOUGHTON. To just take a scythe right across the budget and then start putting things back according to what the specific need is; is that right?

Mr. REISCHAUER. Yes. I mean, this is not a well thought out plan. I have just come up with this right now.

But I think you are in an impossible situation when you say we want to balance the budget but we don't want to increase taxes. We want to take Social Security off, and we want to make sure defense doesn't decline in real terms from where it is now, and we can't touch civil service and military pensions, and we really can't touch veterans, and we probably can't touch unemployment compensation because it is really State money.

Of course, you can't do much about interest. At this point the game is over, because the implied cuts on everything else in the budget are so draconian that no one will agree to cooperate. I am saying that it is very easy to take things off the table if there is no price imposed on you when you take it off. All you do is receive thank-you letters from the Social Security recipients: thank you for taking this off the table.

Mr. HOUGHTON. Just one other question: capital budgeting. As industry does it, not throwing in human resources and things like that, when we are talking about investing it is very difficult for a government agency to invest it. What do you think about that?

Mr. REISCHAUER. As an institution, we have never been enamored with the idea. Most people bring it forward as a proposal that they believe would mean that the amount of deficit reduction that we had to do was reduced. The analysis we have done of it suggests that that is not the case, that if you correctly counted the depreciation of the existing capital stock of the Federal Government and included that as an expenditure item in the budget, the deficit would in fact look a lot different from what it appears to be right now.

There are some very difficult issues, of course, about the definition of capital, and there is concern that the definition would be abused by the Congress and the executive branch.

Mr. HOUGHTON. Thank you.

Mr. MCCRERY. Thank you, Mr. Houghton. Thank you, Dr. Reischauer, very much for your testimony.

Mr. REISCHAUER. Thank you.

[Whereupon, at 2:50 p.m., the hearing was adjourned.]

[A submission for the record follows:]

Public Service Commission
State of North Dakota

COMMISSIONERS

Leo M. Reinboid
President
Susan E. Wefald
Bruce Hagen

600 E. Boulevard
Bismarck, North Dakota 58505
701-224-2400
Toll Free in ND 800-932-2400
FAX 701-224-2410
TDD 701-224-4065

Executive Secretary
Jon H. Mielke

February 10, 1995

The Honorable Bill Archer
Chairman
Committee on Ways and Means
Room 1102, Longworth House Office Building
Washington, D.C. 20515

Dear Congressman Archer:

I would like to comment for the printed record of the February 7, 1995 hearing on the President's fiscal year 1996 budget. I know there are many items to discuss on the budget, but there are several areas I believe your Committee also should consider.

In most of the public comments made so far regarding the 1996 budget and future budgets, there is much discussion about down-sizing government, eliminating waste, bringing the annual budget deficit under control, and, hopefully, starting to pay down on the national debt. All of this is fine, but generally missing is any serious discussion on reining in the enormous amounts of money spent to operate the Central Intelligence Agency.

We are a democracy, and the Cold War is over. I believe an Intelligence Agency can be justified in the national interest. I also believe reasonable spending for its operation is justified, but the Agency should be made more efficient and open much of its actions to the public. Democracies need open government--not a bunch of "spooks" who often try to oppose changes in the governments of other countries rather than truly just being an information gathering Intelligence Agency. I am sure billions of dollars could be saved annually by reducing the Central Intelligence Agency budget if you are serious about making government more efficient and balancing the budget.

The Ways and Means Committee should also look at military pensions. It makes no sense to me to allow someone to enter the military in their teens, finish service in their 30s, and begin to draw a pension. Military pensions should begin at age 65. A second problem with pensions, as I understand it, is that the funding for pensions comes right out of the general funds of the United States. Does the military have a pension fund that they contribute to from day-one of their service just like other government employees? If not, why not?

I believe where our government provides a service, a better effort should be made to recover the costs for that service. For example, fees for use of our national parks and the concessions in them should cover the cost of maintaining and improving our parks.

There is a huge amount of government subsidies, special tax benefits, to many special interests. To be fair, all of them should be on the table. For example, as I understand it, our tax system subsidizes Sunkist, Gallo, and McDonald's to advertise their products abroad; some private forestry companies owe tax payers for timber purchased but not paid for; and some mining companies pay pennies for title to the United States people's land that is worth millions.

There is a lot of discussion in Congress about reforming "welfare" to cut off benefits to millions of poor children. I believe Congress also should reform the benefits given to corporations that receive special tax benefit welfare.

Your Committee has a difficult task, but I sincerely believe the annual budget of the United States should be balanced right now and everything should be on the table. A balanced budget amendment is a cop-out for balancing the budget in the future instead of just doing it now.

We live in a great, free, open democracy and a government of the people, by the people and for the people. The American people want a fair system where the poor and middle class are not ignored by Congress and get as much consideration as corporations that are on welfare.

Thank you for the opportunity to present my views.

Sincerely,

Bruce Hagen

Bruce Hagen
Commissioner

BH/cm